

## **Management's Discussion and Analysis**

This Management's Discussion and Analysis ("MD&A") comments on the operations, performance and financial condition of Toromont Industries Ltd. ("Toromont" or the "Company") as at and for the year ended December 31, 2017, compared to the preceding year. This MD&A should be read in conjunction with the audited consolidated financial statements and related notes for the year ended December 31, 2017.

The consolidated financial statements reported herein have been prepared in accordance with International Financial Reporting Standards ("IFRS") and are reported in Canadian dollars. The information in this MD&A is current to February 22, 2018.

### **Advisory**

Information in this MD&A that is not a historical fact is "forward-looking information". Words such as "plans", "intends", "outlook", "expects", "anticipates", "estimates", "believes", "likely", "should", "could", "will", "may" and similar expressions are intended to identify statements containing forward-looking information. Forward-looking information in this MD&A reflect current estimates, beliefs, and assumptions, which are based on Toromont's perception of historical trends, current conditions and expected future developments, as well as other factors management believes are appropriate in the circumstances. Toromont's estimates, beliefs and assumptions are inherently subject to significant business, economic, competitive and other uncertainties and contingencies regarding future events and as such, are subject to change. Toromont can give no assurance that such estimates, beliefs and assumptions will prove to be correct. This MD&A also contains forward-looking statements about the recently acquired businesses of Hewitt.

Numerous risks and uncertainties could cause the actual results to differ materially from the estimates, beliefs and assumptions expressed or implied in the forward-looking statements, including, but not limited to: business cycles, including general economic conditions in the countries in which Toromont operates; commodity price changes, including changes in the price of precious and base metals; changes in foreign exchange rates, including the Cdn\$/US\$ exchange rate; the termination of distribution or original equipment manufacturer agreements; equipment product acceptance and availability of supply; increased competition; credit of third parties; additional costs associated with warranties and maintenance contracts; changes in interest rates; the availability of financing; potential environmental liabilities of the acquired businesses and changes to environmental regulation; failure to attract and retain key employees; damage to the reputation of Caterpillar, product quality and product safety risks which could expose Toromont to product liability claims and negative publicity; new, or changes to current, federal and provincial laws, rules and regulations including changes in infrastructure spending; and any requirement of Toromont to make contributions to the registered funded defined benefit pension plans, postemployment benefits plan or the multi-employer pension plan obligations in which it participates in and acquired from Hewitt thereunder in excess of those currently contemplated. Risks and uncertainties related to the acquisition of the Hewitt operations could also cause the actual results to differ materially from the estimates beliefs and assumptions expressed or implied in the forward-looking statements, including but not limited to: changes in consumer and business confidence as a result of the change in ownership; the potential for liabilities assumed in the acquisition to exceed our estimates or for material undiscovered liabilities in the Hewitt business; the potential for third parties to terminate or alter their agreements or relationships with Toromont as a result of the acquisition; and risks related

to integration of Hewitt operations with those of Toromont including cost of integration and ability to achieve the expected benefits. Readers are cautioned that the foregoing list of factors is not exhaustive.

Any of the above mentioned risks and uncertainties could cause or contribute to actual results that are materially different from those expressed or implied in the forward-looking information and statements included in this MD&A. For a further description of certain risks and uncertainties and other factors that could cause or contribute to actual results that are materially different, see the risks and uncertainties set out in the "Risks and Risk Management" and "Outlook" sections herein. Other factors, risks and uncertainties not presently known to Toromont or that Toromont currently believes are not material could also cause actual results or events to differ materially from those expressed or implied by statements containing forward-looking information.

Readers are cautioned not to place undue reliance on statements containing forward-looking information, which reflect Toromont's expectations only as of the date of this MD&A, and not to use such information for anything other than their intended purpose. Toromont disclaims any obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise, except as required by law.

## **CORPORATE DEVELOPMENT**

### **Acquisition of the Hewitt Group of Companies ("Hewitt")**

On October 27, 2017, Toromont completed the acquisition of the businesses and net operating assets of Hewitt.

Hewitt was the authorized Caterpillar dealer for the province of Québec, Western Labrador and the Maritimes, as well as the Caterpillar lift truck dealer for Québec and most of Ontario, in addition to the MaK engine dealer for Québec, the Maritimes and the Eastern seaboard of the United States, from Maine to Virginia. Additional distribution rights were also acquired in this transaction.

This important transaction delivers a substantial growth opportunity, and strengthens the Company's expertise and operations in the mining, construction, power systems, product support and expanded product lines.

For further information on the accounting for the acquisition, refer to note 3 of the notes to the consolidated financial statements.

## **CORPORATE PROFILE AND BUSINESS SEGMENTATION**

As at December 31, 2017, Toromont employed approximately 6,000 people in 146 locations across Canada and the United States. Toromont is listed on the Toronto Stock Exchange under the symbol TIH.

Toromont has two reportable operating segments: the Equipment Group and CIMCO.

The Equipment Group includes Toromont CAT, one of the world's larger Caterpillar dealerships, Battlefield – The CAT Rental Store, an industry-leading rental operation, Sitech, providing Trimble technology products and services, AgWest, an agricultural equipment and solutions dealer representing AGCO, CLAAS and other manufacturers' products, in addition to the recently acquired businesses, which are in varying stages of integration. Performance in the Equipment Group is driven by activity in several industries: road building and other infrastructure-related activities; mining; residential and commercial construction; power generation; aggregates; waste management; steel; forestry; and agriculture. Significant activities include the sale, rental and service of mobile equipment for Caterpillar and other manufacturers; sale, rental and service of engines used in a variety of applications including industrial, commercial, marine, on-highway trucks and power generation; and sale of complementary and related products, parts and service. Pursuant to the acquisition, the Company is now the exclusive Caterpillar dealer for a contiguous geographical territory in Canada that covers Manitoba, Ontario, Quebec, Newfoundland, New Brunswick, Nova Scotia, Prince Edward Island and most of Nunavut. Additionally, the Company is now the MaK engine dealer for the Eastern seaboard of the United States, from Maine to Virginia.

CIMCO is a market leader in the design, engineering, fabrication, installation and after-sale support of refrigeration systems in industrial and recreational markets. Results of CIMCO are influenced by conditions in the primary market segments served: beverage and food processing; cold storage; food distribution; mining; and recreational ice rinks. CIMCO offers systems designed to optimize energy usage through proprietary products such as ECO CHILL<sup>®</sup>. CIMCO has manufacturing facilities in Canada and the United States and sells its solutions globally.

## **PRIMARY OBJECTIVE AND MAJOR STRATEGIES**

The primary objective of the Company is to build shareholder value through sustainable and profitable growth, supported by a strong financial foundation. To guide its activities in pursuit of this objective, Toromont works toward specific, long-term financial goals (see section heading "Key Performance Measures" in this MD&A) and each of its operating groups consistently employs the following broad strategies:

### **Expand Markets**

Toromont serves diverse markets that offer significant long-term potential for profitable expansion. Each operating group strives to achieve or maintain leading positions in markets served. Incremental revenues are derived from improved coverage, market share gains and geographic expansion. Expansion of the installed base of equipment provides the foundation for product support growth and leverages the fixed costs associated with the Company's infrastructure.

## **Strengthen Product Support**

Toromont's parts and service business is a significant contributor to overall profitability and serves to stabilize results through economic downturns. Product support activities also represent opportunities to develop closer relationships with customers and differentiate the Company's product and service offering. The ability to consistently meet or exceed customers' expectations for service efficiency and quality is critical, as after-market support is an integral part of the customer's decision-making process when purchasing equipment.

## **Broaden Product Offerings**

Toromont delivers specialized capital equipment to a diverse range of customers and industries. Collectively, hundreds of thousands of different parts are offered through the Company's distribution channels. The Company expands its customer base through selectively extending product lines and capabilities. In support of this strategy, Toromont represents product lines that are considered leading and generally best-in-class from suppliers and business partners who continually expand and develop their offerings. Strong relationships with suppliers and business partners are critical in achieving growth objectives.

## **Invest in Resources**

The combined knowledge and experience of Toromont's people is a key competitive advantage. Growth is dependent on attracting, retaining and developing employees with values that are consistent with Toromont's. A highly principled culture, share ownership and profitability-based incentive programs result in a close alignment of employee and shareholder interests. By investing in employee training and development, the capabilities and productivity of employees continually improve to better serve shareholders, customers and business partners.

Toromont's information technology represents another competitive differentiator in the marketplace. The Company's selective investments in technology, inclusive of e-commerce initiatives, strengthen customer service capabilities, generate new opportunities for growth, drive efficiency and increase returns to shareholders.

## **Maintain a Strong Financial Position**

A strong, well-capitalized balance sheet creates stability and financial flexibility, and has contributed to the Company's long-term track record of profitable growth. It is also fundamental to the Company's future success.

## CONSOLIDATED ANNUAL OPERATING RESULTS

<i>(\$ thousands, except per share amounts)</i>	2017	2016	\$ change	% change
<b>REVENUES</b>	<b>\$ 2,350,162</b>	\$ 1,912,040	\$ 438,122	23%
Cost of goods sold	<b>1,794,213</b>	\$ 1,443,978	350,235	24%
Gross profit <sup>(1)</sup>	<b>555,949</b>	468,062	87,887	19%
Selling and administrative expenses	<b>306,367</b>	256,438	49,929	19%
Gain on sale of internally-developed software	-	(4,939)	4,939	nm
<b>OPERATING INCOME <sup>(1)</sup></b>	<b>249,582</b>	216,563	33,019	15%
Interest expense	<b>12,277</b>	7,242	5,035	70%
Interest and investment income	<b>(4,659)</b>	(4,006)	(653)	16%
Income before income taxes	<b>241,964</b>	213,327	28,637	13%
Income taxes	<b>65,994</b>	57,579	8,415	15%
<b>NET EARNINGS</b>	<b>175,970</b>	155,748	20,222	13%
<b>BASIC EARNINGS PER SHARE</b>	<b>\$ 2.22</b>	\$ 1.99	\$ 0.23	12%
<b>KEY RATIOS:</b>				
Gross profit margin <sup>(1)</sup>	<b>23.7%</b>	24.5%		
Selling and administrative expenses as a % of revenues	<b>13.0%</b>	13.4%		
Operating income margin <sup>(1)</sup>	<b>10.6%</b>	11.3%		
Income taxes as a % of income before income taxes	<b>27.3%</b>	27.0%		
Return on capital employed <sup>(1)</sup>	<b>21.5%</b>	24.5%		
Return on equity <sup>(1)</sup>	<b>19.3%</b>	20.0%		

(1) Defined in the section titled "Description of Additional GAAP and Non-GAAP Measures".

The Company delivered another solid year, both in terms of incremental volumes and profit generated by the acquired businesses, and on solid organic growth generated by the legacy Equipment Group businesses and CIMCO.

For the remainder of this document, unless otherwise indicated, specific comments on operating results will refer to the legacy Toromont businesses only. Where applicable, the acquired businesses will be referred to collectively as Toromont Quebec/Maritimes ("Toromont QM").

Toromont QM generated revenues of \$242.6 million for the two months since acquisition. Excluding this, revenues grew 10% or \$195.5 million to \$2.1 billion. The Equipment Group reported a 10% increase on strong equipment sales and rentals along with continued product support growth. CIMCO also reported strong growth of 13% on record package sales and product support revenues.

Gross profit margin was lower by 80 basis points ("bps"), half of which related to lower average profit margins in Toromont QM. In the Equipment Group, challenging market conditions continued to exert downward pressures on equipment margins. At CIMCO, higher package margins served to offset lower product support margins. Across both Groups, a higher proportion of equipment revenues to higher margin product support revenues dampened overall margins.

Selling and administrative expenses increased \$49.9 million or 19% reflecting the incremental expenses at Toromont QM for the two months (\$38.0 million), higher compensation costs (up \$5.6 million), acquisition-related expenses (\$6.0 million) and higher mark-to-market adjustments on Deferred Share Units ("DSUs") (up \$0.9 million). Most other expense categories were lower

as the Company remains focused on expense management. Excluding Toromont QM and acquisition-related expenses, selling and administrative expenses as a percentage of revenues were 100 bps lower (12.4% versus 13.4%).

A gain of \$4.9 million on the sale of internally-developed software was recorded in 2016.

Interest expense increased as a result of the debenture offerings and amendments to the credit facility to partially fund the acquisition.

Interest income increased on higher investment income resulting from higher average cash balances held in anticipation of the acquisition, partially offset by lower interest from conversions of equipment on rent with a purchase option ("RPO"). RPO interest income varies based on the length of the rental period to conversion.

The effective income tax rate for 2017 was 27.3% compared to 27.0% in 2016.

Net earnings in 2017 were \$176.0 million, up 13% from 2016 while basic earnings per share ("EPS") increased \$0.23 or 12% to \$2.22.

Excluding all impact of the acquisition of Toromont QM together with the software gain in 2016, net earnings increased 16% while EPS increased 15%.

Comprehensive income in 2017 was \$168.2 million (2016 - \$154.2 million), comprised mainly of net earnings and other comprehensive loss resulting from an actuarial loss on defined benefit pension and other post-employment benefit plans and an unfavorable change in the fair value of cash flow hedges.

## **BUSINESS SEGMENT ANNUAL OPERATING RESULTS**

The accounting policies of the segments are the same as those of the consolidated entity. Management evaluates overall business segment performance based on revenue growth, operating income relative to revenues and return on capital employed. Corporate expenses are allocated based on each segment's revenue. Interest expense and interest and investment income are not allocated.

## Equipment Group

(\$ thousands)	2017	2016	\$ change	% change
Equipment sales and rentals				
New	\$ 784,915	\$ 524,931	\$ 259,984	50%
Used	227,293	239,446	(12,153)	(5%)
Rentals	261,641	221,009	40,632	18%
Total equipment sales and rentals	1,273,849	985,386	288,463	29%
Power generation	11,270	12,242	(972)	(8%)
Product support	746,832	634,018	112,814	18%
<b>Total revenues</b>	<b>\$ 2,031,951</b>	<b>\$ 1,631,646</b>	<b>\$ 400,305</b>	<b>25%</b>
<b>Operating income</b>	<b>\$ 219,814</b>	<b>\$ 196,124</b>	<b>\$ 23,690</b>	<b>12%</b>
<b>Capital expenditures:</b>				
Rental	\$ 102,343	\$ 98,668	\$ 3,675	4%
Other	35,888	22,938	12,950	56%
<b>Total</b>	<b>\$ 138,231</b>	<b>\$ 121,606</b>	<b>\$ 16,625</b>	<b>14%</b>
<b>KEY RATIOS:</b>				
Product support revenues as a % of total revenues	36.8%	38.9%		
Operating income margin	10.8%	12.0%		
Group total revenues as a % of consolidated revenues	86.5%	85.3%		
Return on capital employed	19.3%	21.8%		

The Equipment Group results reflect good year-over-year growth for the legacy businesses and two months of operations at Toromont QM.

New equipment sales in the legacy businesses rebounded from a soft year in 2016 to record levels. Conversely, used equipment sales returned to normal levels following a record year in 2016. There is interplay between new and used equipment sales reflecting market conditions, equipment availability and relative pricing. On a combined basis, equipment sales increased \$110.4 million or 14% at the legacy businesses as described below. Equipment sales at Toromont QM were \$137.4 million.

Sales into legacy mining markets increased 74% versus last year. Mining activity within our territories remained active, providing opportunities for sales to support mine expansion, equipment replacement and new mine development. Toromont's proven track record in this sector again led to several key wins during the year. Power systems reported strong year-over-year growth of 51%. Demand for alternative sources of energy as a result of escalating electricity costs in Ontario, in addition to the construction of large data centers in our territories fuelled growth. Agriculture equipment sales increased 14%. Construction market sales contracted slightly (2%) as all regions except Manitoba and the Arctic reported declines.

Rental revenues at the legacy businesses increased \$22.0 million or 10% versus last year. Heavy equipment rentals were up 17% on improved utilization and a larger fleet. Higher activity levels in Newfoundland and Manitoba were partially offset by a decline in Ontario which faced softer market conditions. Light equipment rentals were up 9% with all regions reporting growth. Power rentals increased 33%, driven by strong demand for uninterrupted power supply/generators, pumps and temperature control units. Focus remains on growing and diversifying the power fleet offering. Rental revenues from RPO (equipment on rent with a

purchase option) were up 1%. The RPO fleet at December 31, 2017, was \$57.2 million versus \$61.0 million at the end of 2016. Rental revenues at Toromont QM were \$18.6 million with an RPO fleet at December 31, 2017 of \$14.4 million.

Power generation revenues from Toromont owned-and-managed plants decreased \$1.0 million or 8% over last year. The decrease was mainly attributable to lower electricity and thermal revenues at the Sudbury Hospital plant.

Product support revenues at the legacy businesses increased \$26.2 million or 4% reflecting strong rebuild activity. Parts revenues were up 4% with good growth in most market segments. Service revenues were up 6% reflecting strong mining activity which served to offset decreases in other segments. As previously reported, Caterpillar's discontinuation of the on-highway truck product line a few years ago has led to a gradual reduction of product support opportunities in this space. Product support revenues at Toromont QM were \$86.6 million.

Gross margins decreased 130 bps versus last year. Lower average profitability at Toromont QM reduced overall margins by 50 bps. Other than this, lower equipment margins (down 70 bps) and an unfavorable sales mix of product support revenues to total revenues (down 40 bps) were partially offset by improved product support margins (up 30 bps). A very tight pricing environment exacerbated by reduced rental conversions and a lower mix of higher margin used equipment sales exerted downward pressures on equipment margins for most of the year.

Selling and administrative expenses increased \$6.9 million or 3% compared to last year, excluding Toromont QM. Higher compensation costs, including the mark-to-market on DSUs (up \$2.5 million) and acquisition-related expenses (\$6.0 million) were partially offset by a gain on sale of certain assets (\$2.6 million). As a percentage of revenues, expenses were 80 bps lower than 2016 (12.3% vs. 13.1%) after excluding Toromont QM and acquisition-related expenses.

Operating income increased \$23.7 million or 12%. Excluding all impact from the Toromont QM acquisition in 2017, together with the previously described gain on sale of internally-developed software recorded in 2016, underlying operating income increased \$24.0 million or 13% and was 30 bps higher as a percentage of revenues (12.0% versus 11.7% last year).

Capital expenditures in the legacy Equipment Group were \$8.2 million (7%) higher year-over-year, while \$8.4 million was invested at Toromont QM. Replacement and expansion of the rental fleet, net of dispositions, accounted for \$69.5 million of total investment in 2017. Other capital expenditures include \$15.8 million for new and expanded facilities to meet current and future growth requirements, \$12.5 million for service and delivery vehicles, \$4.6 million for machinery and equipment and \$1.9 million for upgrades and enhancements to the information technology infrastructure.

## Bookings and Backlogs

<i>(\$ millions)</i>	<b>2017</b>	2016	\$ change	% change
Bookings - year ended December 31	<b>\$ 1,013</b>	\$ 814	\$ 199	24%
Backlogs - as at December 31	<b>\$ 327</b>	\$ 147	\$ 180	122%

Bookings included \$86.3 million for the two months of operations at Toromont QM. Excluding these, bookings increased 14% principally due to higher mining (up 45%), power systems (up 37%), construction (up 5%) and agriculture orders (up 6%).

Backlogs increased to \$327.0 million, including \$128.3 million at Toromont QM. At December 31, 2017, the majority of the backlog related to construction (37%), power systems (33%), mining (20%) and agriculture (8%), most of which is expected to be delivered in 2018. Backlogs can vary significantly from period to period on large project activities, especially in mining and power systems, the timing of orders and deliveries and the availability of equipment from either equipment or suppliers.

## CIMCO

<i>(\$ thousands)</i>	<b>2017</b>	2016	\$ change	% change
Package sales	<b>\$ 189,212</b>	\$ 161,614	\$ 27,598	17%
Product support	<b>128,999</b>	118,780	10,219	9%
<b>Total revenues</b>	<b>\$ 318,211</b>	\$ 280,394	\$ 37,817	13%
<b>Operating income</b>	<b>\$ 29,768</b>	\$ 20,439	\$ 9,329	46%
<b>Capital expenditures</b>	<b>\$ 1,429</b>	\$ 1,888	\$ (459)	(24%)
<b>KEY RATIOS:</b>				
Product support revenues as a % of total revenues	<b>40.5%</b>	42.4%		
Operating income margin	<b>9.4%</b>	7.3%		
Group total revenues as a % of consolidated revenues	<b>13.5%</b>	14.7%		
Return on capital employed	<b>96.4%</b>	73.8%		

CIMCO delivered another record year on continued growth in Canada and the US. Translation of US operations did not have a significant impact on trends.

Package revenues reflect the progress of project construction applying the percentage-of-completion method for revenue recognition. This introduces a degree of variability as the timing of projects and construction schedules are largely under the control of third parties (contractors and end-customers). In Canada, package revenues were up \$20.2 million or 17%, reflecting strong sales into recreational markets (up 95%), partially offset by softer industrial activity (down 5%). Good growth was reported in Ontario and Atlantic Canada, while Quebec was lower following record activity levels in 2016. In the US, package revenues increased \$7.4 million or 18% on higher sales into recreational markets (up 27%).

Product support revenues increased \$10.2 million or 9% versus last year, reflecting growth in Canada (up 11%) while US revenues were relatively unchanged. The increased installed base provides a solid growth platform in both Canada and the US.

Gross margins increased 180 bps on higher package margins, partially offset by lower product support margins and an unfavorable sales mix of product support revenues to total revenues. Improved package margins reflect improved execution and lower warranty costs. Product support revenues were 40.5% as a percentage of total revenues in 2017 compared to 42.4% in 2016.

Selling and administrative expenses increased \$4.8 million or 11% compared to last year. Higher compensation costs (up \$4.1 million) on annual salary increases, additional headcount to support growth and increased profit sharing accrual on the higher earnings accounted for the majority of the increase. As a percentage of revenues, expenses were 30 bps lower than last

year (15.0% vs. 15.3%).

Operating income increased 46% to \$29.8 million largely reflecting the higher revenues and gross profit margins together with a lower expense ratio. As a percentage of revenues, operating income increased 210 bps to 9.4%.

Capital expenditures were down 24% to \$1.4 million with the majority of expenditures in 2017 related to additional service vehicles (\$0.6 million), information technology infrastructure enhancements and upgrades (\$0.3 million) and machinery and equipment (\$0.2 million).

### **Bookings and Backlogs**

(\$ millions)	2017	2016	\$ change	% change
Bookings - year ended December 31	\$ 233	\$ 178	\$ 55	31%
Backlogs - as at December 31	\$ 134	\$ 99	\$ 35	35%

Bookings of \$233.0 million surpassed the all-time high set last year. Industrial bookings were up 41% with good growth in Canada (up 39%) and the US (up 50%). Recreational bookings increased 15% with strong Canadian activity levels (up 50%) offsetting lower US levels (down 28%).

Backlogs increased \$35.0 million or 35% to \$134.0 million. Industrial backlogs were up 68% with terrific growth in Canada (up 84%), partially offset by a slight decline in the US (down 4%). Recreational backlogs were relatively unchanged year-over-year as higher Canadian activity levels (up 3%) were offset by lower US levels (down 4%). The record backlog levels for this time of year provide a solid base entering 2018 with substantially all expected to be realized as revenue during 2018.

### **CONSOLIDATED FINANCIAL CONDITION**

The Company has maintained a strong financial position for many years and continues to do so, even after raising financing for the substantial acquisition completed this year.

At December 31, 2017, the ratio of net debt to total capitalization was 40%.

### **Non-Cash Working Capital**

The Company's investment in non-cash working capital was \$619.8 million at December 31, 2017. The major components, along with the changes from December 31, 2016, are identified in the following table.

<i>(\$ thousands)</i>	<b>2017</b>	2016	<b>\$ change</b>	<b>% change</b>
Accounts receivable	\$ 528,748	\$ 260,691	\$ 268,057	103%
Inventories	780,024	435,757	344,267	79%
Other current assets	8,386	5,236	3,150	60%
Accounts payable and accrued liabilities	(521,666)	(231,746)	(289,920)	125%
Provisions	(17,436)	(16,094)	(1,342)	8%
Income taxes payable	(204)	(1,262)	1,058	nm
Derivative financial instruments	(5,260)	1,197	(6,457)	nm
Dividends payable	(15,655)	(14,110)	(1,545)	11%
Deferred revenues	(137,129)	(51,211)	(85,918)	168%
<b>Total non-cash working capital</b>	<b>\$ 619,808</b>	<b>\$ 388,458</b>	<b>\$ 231,350</b>	<b>60%</b>

Accounts receivable increased \$268.1 million of which \$182.9 million related to Toromont QM and \$42.7 million related to amounts owing to the Company as part of the acquisition of Hewitt (refer to note 4 of the notes of the consolidated financial statements). For the legacy businesses, accounts receivable were up \$42.5 million or 16% compared to 2016 largely reflecting the 18% increase in revenues in the quarter. Equipment Group accounts receivable increased \$19.9 million or 10% while CIMCO accounts receivable increased \$22.6 million or 44%.

Inventories increased \$344.3 million of which \$278.9 million related to Toromont QM. For the legacy businesses, inventories were up \$65.4 million or 15% with increases in both Groups.

- Equipment Group inventories were \$63.4 million or 15% higher than this time last year with increases in equipment (up \$50.4 million or 17%), parts (up \$7.0 million or 7%) and service work-in-process (up \$6.0 million or 37%). The higher equipment inventory levels were mainly a result of certain inventories held in advance of customer-specified delivery dates later in 2018, while the higher service work-in-process reflects busy shops.
- CIMCO inventories were \$2.0 million (11%) higher than this time last year, reflecting strong work-in-process levels.

The increase in other current assets mainly relates to prepaid expenses at Toromont QM.

Accounts payable and accrued liabilities increased \$289.9 million of which \$166.4 million related to Toromont QM. For the legacy businesses, the increase of \$123.5 million or 53% versus this time last year mainly reflects:

- The timing of payments and terms related to inventory purchases and other supplies;
- Higher DSU liability primarily attributable to the higher average share price, partly due to the acquisition announcement; and
- Higher accrual for performance incentive bonuses on the higher income.

Income taxes payable reflects the difference between tax installments and current tax expense.

Derivative financial instruments represent the fair value of foreign exchange contracts. Fluctuations in the value of the Canadian dollar have led to a cumulative net loss of \$5.3 million as at December 31, 2017. This is not expected to affect net income as the unrealized losses will offset future gains on the related hedged items.

Higher dividends payable year over year reflect the higher dividend rate and additional dividends on the shares issued to partially fund the acquisition. In 2017, the quarterly dividend rate was increased from \$0.18 per share to \$0.19 per share, a 6% increase. As part of the

acquisition, 2,249,478 common shares were issued (refer to note 3 of the notes to the consolidated financial statements).

Deferred revenues represent billings to customers in excess of revenue recognized. In the Equipment Group, deferred revenues arise on sales of equipment with residual value guarantees, extended warranty contracts and other long-term customer support agreements as well as on progress billings on long-term construction contracts. Excluding \$50.6 million of deferred revenues at Toromont QM, Equipment Group deferred revenues were up 62% versus last year due to increased progress billings for equipment deliveries later in the year and progress billings relative to work completed on long-term customer service agreements (“CSAs”). In CIMCO, deferred revenues arise on progress billings in advance of revenue recognition and were up 85% versus last year, reflecting the strong backlog levels.

### **Goodwill and Intangibles**

The Company performs impairment tests on its goodwill and intangibles with indefinite lives on an annual basis or as warranted by events or circumstances. The assessment entails estimating the fair value of operations to which the goodwill and intangibles relate, using the present value of expected discounted future cash flows. This assessment affirmed goodwill and intangibles values as at December 31, 2017 for balances existing at the beginning of the year and goodwill and intangibles acquired as part of the acquisition. See note 8 of the notes to the consolidated financial statements.

### **Employee Share Ownership**

The Company employs a variety of stock-based compensation plans to align employees’ interests with corporate objectives.

The Company maintains an Executive Stock Option Plan for its senior employees. Non-employee directors have not received grants under this plan since 2013. Stock options vest 20% per year on each anniversary date of the grant and are exercisable at the designated common share price, which is fixed at prevailing market prices at the date the option is granted. Stock options granted in 2013 and after have a 10-year term while those granted prior to 2013 have a seven-year term. At December 31, 2017, 2.6 million options to purchase common shares were outstanding, of which 1.1 million were exercisable.

The Company offers an Employee Share Purchase Plan whereby employees can purchase shares by way of payroll deductions. At December 31, 2017, employees of Toromont QM were not yet eligible to participate in this plan. Under the terms of this plan, eligible employees may purchase common shares of the Company in the open market at the then-current market price. The Company pays a portion of the purchase price, matching contributions at a rate of \$1 for every \$3 contributed, to a maximum of the greater of 2.5% of an employee’s base salary or \$1,000 per annum. Company contributions vest to the employee immediately. Company contributions amounting to \$2.0 million in 2017 (2016 – \$1.8 million) were charged to selling and administrative expense when paid. Approximately 52% (2016 – 50%) of eligible employees participate in this plan. The Plan is administered by an independent third party.

The Company also offers a deferred share unit (“DSU”) plan for certain executives and non-employee directors, whereby they may elect, on an annual basis, to receive all or a portion of their performance incentive bonus or fees, respectively, in DSUs. Non-employee directors also receive DSUs as part of their compensation, aligning at-risk and cash compensation

components. A DSU is a notional unit that reflects the market value of a single Toromont common share and generally vests immediately. DSUs will be redeemed on cessation of employment or directorship. DSUs have dividend equivalent rights, which are expensed as earned. The Company records the cost of the DSU plan as compensation expense in selling and administrative expenses.

As at December 31, 2017, 426,279 DSUs were outstanding with a total value of \$23.4 million (2016 – 407,731 units at a value of \$17.3 million). The liability for DSUs is included in accounts payable and accrued liabilities on the consolidated statement of financial position.

## **Employee Future Benefits**

### Defined Contribution Plans

The Company sponsors pension arrangements for substantially all of its employees, primarily through defined contribution plans in Canada and a 401(k) matched savings plan in the United States. Certain unionized employees do not participate in Company-sponsored plans, and contributions are made to their retirement programs in accordance with the respective collective bargaining agreements. In the case of defined contribution plans, regular contributions are made to the individual employee accounts, which are administered by a plan trustee in accordance with the plan documents. At December 31, 2017, acquired employees at Toromont QM were not part of these plans.

### Defined Benefit Plans

#### Pre-acquisition

The Company sponsors defined benefit pension plans (Powell Plan, Executive Plan and Toromont Plan) for approximately 91 qualifying employees. The Powell and Toromont Plans are administered by a separate Fund that is legally separated from the Company and as described in note 19 of the notes to the consolidated financial statements.

The funded status of these plans changed by \$1.0 million (a decrease in the accrued pension liability) as at December 31, 2017.

The Executive Plan is a supplemental plan and is solely the obligation of the Company. All members of the plan are retired. The Company is not obligated to fund the plan but is obligated to pay benefits under the terms of the plan as they come due. The Company has posted letters of credit to secure the obligations under this plan, which were \$18.4 million as at December 31, 2017. As there are no plan assets, there is no impact on pension expense and contributions.

A key assumption in pension accounting is the discount rate. This rate is set with regard to the yield on high-quality corporate bonds of similar average duration to the cash flow liabilities of the Plans. Yields are volatile and can deviate significantly from period to period.

### Acquisition of Hewitt Plans

The Company acquired defined benefit plans which provides pension and other post-retirement benefits covering approximately 1,800 qualifying employees. The Plans are administered by a separate Fund that is legally separated from the Company and as described in note 19 of the notes to the consolidated financial statements.

The funded status of these plans was a deficit of \$99.8 million as at December 31, 2017.

A key assumption is the discount rate. This rate is set with regard to the yield on high-quality corporate bonds of similar average duration to the cash flow liabilities of the Plans. Yields are volatile and can deviate significantly from period to period.

### **Off-Balance Sheet Arrangements**

Other than the Company's operating leases, the Company does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on its results of operations or financial condition.

### **Legal and Other Contingencies**

Due to the size, complexity and nature of the Company's operations, various legal matters are pending. Exposure to these claims is mitigated through levels of insurance coverage considered appropriate by management and by active management of these matters. In the opinion of management, none of these matters will have a material effect on the Company's consolidated financial position or results of operations.

### **Normal Course Issuer Bid ("NCIB")**

Toromont believes that, from time to time, the purchase of its common shares at prevailing market prices may be a worthwhile investment and in the best interests of both Toromont and its shareholders. As such, the normal course issuer bid with the TSX was renewed in 2017. This issuer bid allows the Company to purchase up to approximately 6.7 million of its common shares, representing 10% of common shares in the public float, in the year ending August 30, 2018. The actual number of shares purchased and the timing of any such purchases will be determined by Toromont. All shares purchased under the bid will be cancelled.

During the year ended December 31, 2017, no shares were purchased and cancelled. During the year ended December 31, 2016, the Company purchased and cancelled 89,244 common shares for \$2.6 million (average cost of \$28.84 per share, including transaction costs).

### **Outstanding Share Data**

As at the date of this MD&A, the Company had 80,951,779 common shares and 2,626,076 share options outstanding.

### **Dividends**

Toromont pays a quarterly dividend on its outstanding common shares and has historically targeted a dividend rate that approximates 30 - 40% of trailing earnings from continuing operations.

During 2017, the Company declared dividends of \$0.76 per common share, \$0.19 per quarter (2016 - \$0.72 per common share or \$0.18 per quarter).

Considering the Company's solid financial position and positive long-term outlook, the Board of Directors announced it is increasing the quarterly dividend to 23 cents per share effective with the dividend payable on April 2, 2018. This represents a 21% increase in Toromont's regular

quarterly cash dividend. The Company has paid dividends every year since going public in 1968 and this represents the 29<sup>th</sup> consecutive year it has announced an increase.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Sources of Liquidity**

Toromont's liquidity requirements can be met through a variety of sources, including cash generated from operations, long- and short-term borrowings and the issuance of common shares. Borrowings are obtained through a variety of senior debentures, notes payable and committed long-term credit facilities.

To partially fund the aforementioned acquisition, the Company expanded and extended its committed unsecured credit facility and issued senior unsecured debentures (refer to note 3 of the notes to the consolidated financial statements for further information).

Effective October 27, 2017, the credit facility provides a term facility of \$250.0 million and a revolving facility of \$500.0 million, maturing in October 2022. Debt under the facility is unsecured and ranks pari passu with debt outstanding under Toromont's existing debentures. The facility includes covenants, restrictions and events of default typical for credit facilities of this nature.

As at December 31, 2017, \$250.0 million was drawn on the facility (2016 - \$nil). Letters of credit utilized an additional \$26.7 million of the facility (2016 - \$21.7 million).

Effective October 27, 2017, the Company also issued senior unsecured debentures in an aggregate principal amount of \$500.0 million (the "Debentures"). The Debentures mature in 2027 and bear interest at a rate of 3.842% per annum, payable semi-annually. The Debentures are unsecured, unsubordinated and rank pari passu with other unsecured, unsubordinated debt.

Cash at December 31, 2017, was \$160.5 million, compared to \$188.7 million at December 31, 2016.

The Company expects that continued cash flows from combined operations in 2018, cash on hand and currently available credit facilities will be more than sufficient to fund requirements for investments in working capital and capital assets.

## Principal Components of Cash Flow

Cash from operating, investing and financing activities, as reflected in the Consolidated Statements of Cash Flows, are summarized in the following table:

<i>(\$ thousands)</i>	<b>2017</b>	2016
<b>Cash, beginning of year</b>	<b>\$ 188,735</b>	\$ 66,680
Cash, provided by (used in):		
<b>Operating activities</b>		
Operations	<b>258,322</b>	215,795
Change in non-cash working capital and other	<b>70,010</b>	34,744
Net rental fleet additions	<b>(66,822)</b>	(61,726)
	<b>261,510</b>	188,813
<b>Investing activities</b>	<b>(979,978)</b>	(18,575)
<b>Financing activities</b>	<b>690,492</b>	(48,112)
Effect of foreign exchange on cash balances	<b>(252)</b>	(71)
(Decrease) increase in cash in the year	<b>(28,228)</b>	122,055
<b>Cash, end of year</b>	<b>\$ 160,507</b>	\$ 188,735

### Cash Flows From Operating Activities

Operating activities provided significantly higher cash flow in 2017 compared to 2016, mainly due to increased cash generation from non-cash working capital and higher net earnings, partially offset by increased investments in net rental fleet additions.

The significant cash inflow from non-cash working capital was mainly due to higher accounts payable and accrued liabilities, deferred revenues and provision for income taxes, partially offset by higher accounts receivable and inventories.

Net rental fleet additions (purchases less proceeds of dispositions) included \$5.8 million spent on growing Toromont QM's fleet. The Company continues to invest heavily in this very important rental segment.

The components and changes in non-cash working capital are discussed in more detail in this MD&A under the heading "Consolidated Financial Condition".

### Cash Flows From Investing Activities

Investing activities used \$980.0 million in 2017 compared to \$18.6 million in 2016, largely reflecting \$945.8 million used to partially fund the acquisition (refer to note 3 of the notes to the consolidated financial statements for further information).

Investments in property, plant and equipment accounted for the remainder of the cash used and included \$2.7 million on facility upgrades and machinery and equipment at the acquired locations. For the legacy businesses, additions included:

- \$14.0 million for land and buildings for new and expanded branches (2016 - \$6.3 million);
- \$13.2 million for service vehicles (2016 - \$12.2 million);
- \$4.1 million for machinery and equipment (2016 - \$3.1 million); and
- \$2.1 million for upgrades and enhancements to information technology infrastructure (2016 - \$1.7 million).

The Company also recorded proceeds on the disposal of internally-developed software of \$4.9 million in 2016.

### **Cash Flows From Financing Activities**

Financing activities provided \$690.5 million versus \$48.1 million used in 2016, largely due to debt, net of financing costs, of \$744.4 million incurred to partially fund the acquisition (refer to note 3 of the notes to the consolidated financial statements for further information).

The Company paid dividends of \$58.9 million or \$0.75 per share in 2017 (2016 - \$55.4 million or \$0.71 per share).

The Company received \$6.8 million on the exercise of stock options in 2017 (2016 - \$11.6 million).

There were no normal course purchases and cancellations of common shares in 2017 compared to 89,244 common shares purchased and cancelled in 2016 for \$2.6 million (average cost of \$28.84, including transaction costs).

## OUTLOOK

The expansion of our territories to include Quebec and Atlantic Canada is expected to be transformative to the long-term performance of Toromont. It provides a substantial growth platform and strengthens our Company by providing a large contiguous operating platform extending across all of Eastern and Central Canada, and into the far North. Effective execution will be required to realize on this significant potential which will allow for a greater combined presence in key Canadian economic sectors such as mining, construction and power systems. Focus is currently on safety of our people, customer deliverables, business integration, and transition to generate favorable long-term returns.

The Equipment Group's parts and service business continues to provide momentum driven by the larger installed base of equipment working in the field, providing a measure of stability in a variable business environment. The Company continues to hire technicians in anticipation of an increase in demand, including the opportunity for increased equipment rebuilds and readying used iron. Broader product lines, investment in rental equipment, expanding the agricultural business and developing product support technologies supporting remote diagnostics and telematics are expected to contribute to longer-term growth.

The long-term outlook for infrastructure spending continues to be positive across most territories.

Increased activity in the mining space has translated to increased bookings and sales this year and we are cautiously optimistic that there is the opportunity for continued growth. In the meantime, production continues at existing mine sites, generating product support opportunities and incremental equipment to support the operations and expansion. With the substantially increased base of installed equipment, product support activity should continue to grow so long as mines remain active.

CIMCO's strong bookings activity and current backlog levels bode well for future prospects. Increasing product support levels is also a positive signal for future trends. CIMCO has a wide product offering using natural refrigerants including innovative CO<sub>2</sub> solutions, which are expected to contribute to growth. In addition, CIMCO is focused on its growth strategy in the US, which represents a significant market opportunity.

The diversity of the markets served, expanding product offering and services, financial strength and disciplined operating culture position the Company for continued growth in the long term.

## CONTRACTUAL OBLIGATIONS

Contractual obligations are set out in the following table. Management believes that these obligations will be met comfortably through cash on hand, cash generated from operations and existing long-term financing facilities.

Payments due by period (\$ thousands)	2018	2019	2020	2021	2022	Thereafter	Total
Long-term debt							
- principal	\$ 1,941	\$ 1,022	\$ -	\$ -	\$ 250,000	\$ 650,000	\$ 902,963
- interest	30,825	30,825	30,825	30,825	29,748	111,342	264,390
Accounts payable	537,321	-	-	-	-	-	537,321
Operating leases	10,725	9,097	5,083	3,488	2,171	1,642	32,206
	<b>\$ 580,812</b>	<b>\$ 40,944</b>	<b>\$ 35,908</b>	<b>\$ 34,313</b>	<b>\$ 281,919</b>	<b>\$ 762,984</b>	<b>\$ 1,736,880</b>

## KEY PERFORMANCE MEASURES

Management reviews and monitors its activities and the performance indicators it believes are critical to measuring success. Some of the key financial performance measures are summarized in the following table. Others include, but are not limited to, measures such as market share, fleet utilization, customer and employee satisfaction, and employee health and safety.

Years ended December 31,	2017	2016	2015	2014	2013
<b>EXPANDING MARKETS AND BROADENING PRODUCT OFFERINGS</b>					
Revenue growth	<b>22.9%</b>	3.5%	11.2%	4.2%	5.7%
Revenue per employee (thousands)	<b>\$ 487</b>	\$ 533	\$ 537	\$ 501	\$ 491
<b>STRENGTHENING PRODUCT SUPPORT</b>					
Product support revenue growth	<b>16.3%</b>	7.6%	24.2%	12.4%	2.5%
<b>INVESTING IN OUR RESOURCES</b>					
Investment in information technology (millions)	<b>\$ 15.0</b>	\$ 15.2	\$ 14.0	\$ 13.4	\$ 12.0
Return on capital employed <sup>(1)</sup>	<b>21.5%</b>	24.5%	24.3%	26.0%	26.5%
<b>STRONG FINANCIAL POSITION</b>					
Non-cash working capital (millions) <sup>(1)</sup>	<b>\$ 620</b>	\$ 388	\$ 421	\$ 335	\$ 282
Net debt to total capitalization <sup>(1)</sup>	<b>40%</b>	-4%	10%	6%	10%
Book value (shareholders' equity) per share	<b>\$ 13.89</b>	\$ 11.29	\$ 9.95	\$ 8.65	\$ 7.50
<b>BUILD SHAREHOLDER VALUE</b>					
Basic earnings per share growth	<b>11.6%</b>	6.3%	8.5%	7.6%	2.9%
Dividends per share growth	<b>5.6%</b>	5.9%	13.3%	15.4%	8.3%
Return on equity <sup>(1)</sup>	<b>19.3%</b>	20.0%	21.6%	23.0%	25.7%

(1) Defined in the section titled "Description of Additional GAAP and Non-GAAP Measures".

Measuring Toromont's results against these strategies over the past five years illustrates that the Company has made and continues to make significant progress. The addition of Toromont QM is expected to further bolster these key performance measures in the near and long-term.

Included in the table above are two months of operations at Toromont QM which increased the income statement metrics presented and conversely diluted the balance sheet metrics. The Company estimates that most metrics improved versus last year on for the legacy businesses.

In relation to the legacy businesses, since 2013, revenues increased at an average annual rate of 7.0%. Revenue per employee in 2017 was \$561. Product support revenue growth has averaged 10.3% annually. This growth has mainly been a result of:

- Increased customer demand in certain market segments, most notably construction and mining;
- Additional product offerings over the years from Caterpillar and other suppliers;
- Organic growth through increased rental fleet size and additional branches;
- Increased customer demand for formal product support agreements;
- Governmental funding programs such as the RinC program which provided support for recreational spending; and
- Acquisitions, primarily within the Equipment Group's rental operations and through business combinations in the agricultural space.

Over the same five-year period, revenue growth has been constrained at times by a number of factors including:

- General economic weakness and uncertainty in specific sectors;
- Competitive conditions;
- Inability to source equipment from suppliers to meet customer demand or delivery schedules; and
- Declines in underlying market conditions such as depressed US industrial markets and Manitoba agricultural markets.

Changes in the Canadian/US exchange rate also affect reported revenues as the exchange rate impacts the purchase price of equipment that, in turn, is reflected in selling prices. Since 2013 there have been fluctuations in the average yearly exchange rate of Canadian dollar against the US dollar – 2013 - US\$0.97, 2014 - US\$0.91, 2015 – US\$0.78, 2016 – US\$0.75 and 2017 – US\$0.77.

Toromont has generated a significant competitive advantage over the past years by investing in its resources, in part to increase productivity levels, and we will continue this into the future as it is a crucial element to our success in the marketplace.

Toromont continues to maintain a strong balance sheet. Leverage, as represented by the ratio of net debt to total capitalization was 40%.

Toromont has paid dividends consistently since 1968 and has increased the dividend in each of the last 29 years. The regular quarterly dividend rate was increased 6% from \$0.18 to \$0.19 per share in 2017 and a further 21% to \$0.23 per share in 2018, evidencing our commitment to delivering exceptional shareholder value.

## CONSOLIDATED FOURTH QUARTER OPERATING RESULTS

Three months ended December 31

(\$ thousands, except per share amounts)

	2017	2016	\$ change	% change
<b>REVENUES</b>	<b>\$ 822,766</b>	\$ 492,223	\$ 330,543	67%
Cost of goods sold	<b>630,652</b>	362,866	267,786	74%
Gross profit	<b>192,114</b>	129,357	62,757	49%
Selling and administrative expenses	<b>105,533</b>	66,469	39,064	59%
<b>OPERATING INCOME</b>	<b>86,581</b>	62,888	23,693	38%
Interest expense	<b>6,788</b>	1,853	4,935	266%
Interest and investment income	<b>(1,637)</b>	(1,377)	(260)	19%
Income before income taxes	<b>81,430</b>	62,412	19,018	30%
Income taxes	<b>22,294</b>	16,883	5,411	32%
<b>NET EARNINGS</b>	<b>\$ 59,136</b>	\$ 45,529	\$ 13,607	30%
<b>BASIC EARNINGS PER SHARE</b>	<b>\$ 0.73</b>	\$ 0.58	\$ 0.15	26%
<b>KEY RATIOS:</b>				
Gross profit margin	<b>23.3%</b>	26.3%		
Selling and administrative expenses as a % of revenues	<b>12.8%</b>	13.5%		
Operating income margin	<b>10.5%</b>	12.8%		
Income taxes as a % of income before income taxes	<b>27.4%</b>	27.1%		

Even excluding the impact of Toromont QM described earlier, the Company delivered record fourth quarter results on solid performance in both Groups.

Toromont QM contributed \$242.6 million to revenues in the fourth quarter. At the legacy businesses, revenues were \$87.9 million or 18% higher with strong growth in both the Equipment Group and CIMCO.

Gross profit margin decreased 300 bps to 23.3% in the quarter. Compressed equipment margins in the Equipment Group, the impact of lower average Toromont QM margins (140 bps) and an unfavorable sales mix of product support revenues to total revenues in both Groups accounted for the majority of the decrease.

Selling and administrative expenses increased \$39.0 million or 59% largely reflecting the incremental expenses at Toromont QM for the two months (\$38.0 million) and acquisition-related expenses (\$3.4 million), partially offset by a lower mark-to-market on DSUs (down \$2.3 million). Excluding Toromont QM and acquisition-related expenses, selling and administrative expenses as a percentage of revenues were down 250 bps to 11.0%.

Interest expense increased as a result of the debenture offerings and amendments to the credit facility to partially fund the acquisition.

Interest income was up from last year on increased investment income from higher average cash balances and higher interest from conversions of equipment on rent with a purchase option.

The effective income tax rate for the fourth quarter of 2017 was 27.4% compared to 27.1% in the same period last year and largely reflects the mix of income by tax jurisdiction.

Net earnings in the quarter were up 30% to \$59.1 million while basic EPS was up 26% to \$0.73.

Excluding all impact of the acquisition of Toromont QM, net earnings increased 25% while EPS increased 21%.

## BUSINESS SEGMENT FOURTH QUARTER OPERATING RESULTS

### Equipment Group

Three months ended December 31				
(\$ thousands)				
	2017	2016	\$ change	% change
Equipment sales and rentals				
New	\$ 308,528	\$ 133,218	\$ 175,310	132%
Used	69,219	66,270	2,949	4%
Rentals	90,039	64,294	25,745	40%
Total equipment sales and rentals	467,786	263,782	204,004	77%
Power generation	2,462	3,137	(675)	(22%)
Product support	255,763	151,874	103,889	68%
<b>Total revenues</b>	<b>\$ 726,011</b>	<b>\$ 418,793</b>	<b>\$ 307,218</b>	<b>73%</b>
<b>Operating income</b>	<b>\$ 75,434</b>	<b>\$ 56,651</b>	<b>\$ 18,783</b>	<b>33%</b>
<b>Bookings (\$ millions)</b>	<b>\$ 328</b>	<b>\$ 224</b>	<b>\$ 104</b>	<b>46%</b>
<b>KEY RATIOS:</b>				
Product support revenues as a % of total revenues	35.2%	36.3%		
Operating income margin	10.4%	13.5%		
Group total revenues as a % of consolidated revenues	88.2%	85.1%		

The Equipment Group reported strong results even after excluding the impact of the two months of operations for Toromont QM.

Combined new and used equipment sales at Toromont QM were \$137.4 million for the two months of operations in the fourth quarter. For the legacy businesses, total equipment sales increased \$40.9 million or 20% versus last year. Deliveries into most market segments were up, led by mining (up 64%), construction (up 7%), agriculture (up 120%) and power systems (up 29%).

Rental revenues at Toromont QM were \$18.6 million. For the legacy businesses, all rental segments reported increases, with light equipment up 10%, heavy equipment up 12%, power rentals up 60% and equipment on rent with a purchase option up 2%. Milder temperatures extended the construction season and led to improved utilization of a larger more rebalanced fleet offering. Power rentals benefitted from activity in support of the Puerto Rico hurricane relief efforts and demand in the cryptocurrency space.

Product support revenues at Toromont QM were \$86.6 million. For the legacy businesses, product support revenues increased \$17.3 million or 11% on higher parts (up 13%) and service revenues (up 8%). Activity levels were good across most segments, notably in mining and construction.

Gross profit margins decreased 340 bps in the quarter versus last year, half of which related to the impact of lower average margins for Toromont QM. For the legacy businesses, lower

equipment margins and an unfavorable sales mix of product support revenues to total revenues were partially offset by slightly higher product support and rental margins.

Selling and administrative expenses increased by \$39.2 million mainly due to the incremental expenses at Toromont QM, acquisition-related expenses and higher compensation costs partially offset by lower mark-to-market on DSUs and a favorable change in the allowance for doubtful accounts resulting from the relative aging profile of accounts receivables. As a percentage of revenues, expenses decreased 210 bps as a percentage of revenues (11.2% vs. 13.3%) after excluding Toromont QM and acquisition-related expenses.

Operating income was up 33% to \$75.4 million in the quarter. Excluding all impact from the Toromont QM acquisition, operating income increased 20% and was 60 bps higher as a percentage of revenues (14.1% versus 13.5% last year).

Excluding Toromont QM, bookings in the fourth quarter of 2017 of \$86.3 million, the legacy businesses grew bookings by \$17.7 million or 8%, with increases in construction, power systems and agriculture orders, partially offset by lower mining orders.

## CIMCO

### Three months ended December 31

(\$ thousands)	2017	2016	\$ change	% change
Package sales	\$ 64,641	\$ 43,152	\$ 21,489	50%
Product support	32,114	30,278	1,836	6%
<b>Total revenues</b>	<b>\$ 96,755</b>	<b>\$ 73,430</b>	<b>\$ 23,325</b>	<b>32%</b>
<b>Operating income</b>	<b>\$ 11,147</b>	<b>\$ 6,237</b>	<b>\$ 4,910</b>	<b>79%</b>
<b>Bookings (\$ millions)</b>	<b>\$ 26</b>	<b>\$ 41</b>	<b>\$ (15)</b>	<b>(37%)</b>
<b>KEY RATIOS:</b>				
Product support revenues as a % of total revenues	33.2%	41.2%		
Operating income margin	11.5%	8.5%		
Group total revenues as a % of consolidated revenues	11.8%	14.9%		

CIMCO delivered record results in the fourth quarter. Translation of US operations did not have a significant impact on results.

Package revenues increased 50% on higher activity in Canada (up 32%) and the US (up 132%). In Canada, with the exception of Atlantic Canada, all regions reported growth, led by Ontario and Quebec. Recreational revenues more than tripled versus last year and were partially offset by softer industrial revenues (down 10%). In the US, both market segments increased considerably with industrial revenues more than tripling and recreational revenues nearly doubling last year's reported amounts for the quarter.

Product support revenues increased 6% versus last year on higher Canadian activity levels as the US remained relatively unchanged.

Gross margins decreased 70 bps principally due to the impact of an unfavorable sales mix of product support revenues to total revenues, partially offset by higher package and product

support margins. Product support revenues as a percentage of total revenues were 33.2% compared to 41.2% in the fourth quarter of 2016.

Selling and administrative expenses were down \$0.2 million or 1% and were 380 bps lower as a percentage of revenues (11.1% versus 14.9% last year). Higher compensation costs were more than offset by decreases across most other expense categories.

Operating income increased 79% to \$11.1 million and was up 300 bps to 11.5% as a percentage of revenues, mainly on the higher revenues and lower relative expense ratio, partially offset by the lower margins.

Bookings in the quarter of \$26.0 million were down 37% versus last year with lower US bookings accounting for approximately 90% of the decrease. Record US bookings in the fourth quarter last year were not repeated.

## QUARTERLY RESULTS

The following table summarizes unaudited quarterly consolidated financial data for the eight most recently completed quarters. This quarterly information is unaudited but has been prepared on the same basis as the 2017 annual audited consolidated financial statements.

<i>(\$ thousands, except per share amounts)</i>	Q1 2017	Q2 2017	Q3 2017	Q4 2017
<b>REVENUES</b>				
Equipment Group	\$ 359,763	\$ 458,158	\$ 488,020	\$ 726,011
CIMCO	52,545	72,772	96,138	96,755
<b>Total revenues</b>	<b>\$ 412,308</b>	<b>\$ 530,930</b>	<b>\$ 584,158</b>	<b>\$ 822,766</b>
<b>NET EARNINGS</b>	<b>\$ 27,024</b>	<b>\$ 40,455</b>	<b>\$ 49,355</b>	<b>\$ 59,136</b>
<b>PER SHARE INFORMATION:</b>				
Basic earnings per share	\$ 0.34	\$ 0.52	\$ 0.63	\$ 0.73
Diluted earnings per share	\$ 0.34	\$ 0.51	\$ 0.62	\$ 0.72
Dividends paid per share	\$ 0.18	\$ 0.19	\$ 0.19	\$ 0.19
Weighted average common shares outstanding - Basic (in thousands)	78,434	78,474	78,522	80,916

<i>(\$ thousands, except per share amounts)</i>	Q1 2016	Q2 2016	Q3 2016	Q4 2016
<b>REVENUES</b>				
Equipment Group	\$ 337,847	\$ 453,145	\$ 421,862	\$ 418,793
CIMCO	50,072	68,979	87,912	73,430
<b>Total revenues</b>	<b>\$ 387,919</b>	<b>\$ 522,124</b>	<b>\$ 509,774</b>	<b>\$ 492,223</b>
<b>NET EARNINGS</b>	<b>\$ 24,170</b>	<b>\$ 38,406</b>	<b>\$ 47,643</b>	<b>\$ 45,529</b>
<b>PER SHARE INFORMATION:</b>				
Basic earnings per share	\$ 0.31	\$ 0.49	\$ 0.61	\$ 0.58
Diluted earnings per share	\$ 0.31	\$ 0.49	\$ 0.60	\$ 0.58
Dividends paid per share	\$ 0.17	\$ 0.18	\$ 0.18	\$ 0.18
Weighted average common shares outstanding - Basic (in thousands)	77,898	78,056	78,211	78,344

Interim period revenues and earnings historically reflect significant variability from quarter to quarter.

The Equipment Group has historically had a distinct seasonal trend in activity levels. Lower revenues are recorded during the first quarter due to winter shutdowns in the construction industry. The fourth quarter had typically been the strongest due in part to the timing of customers' capital investment decisions, delivery of equipment from suppliers for customer-specific orders and conversions of equipment on rent with a purchase option. This pattern is impacted by the timing of significant sales to mining and other customers, resulting from the timing of mine site development and access, and construction project schedules. The Company does not expect this trend to be impacted by the acquisition; however, a better understanding of the customers, industries and economic climate of the new territories is needed before arriving at a conclusion.

CIMCO has also had a distinct seasonal trend in results historically, due to timing of construction activity. Lower revenues are recorded during the first quarter on slower construction schedules due to winter weather. Revenues increase in subsequent quarters as construction schedules ramp up. This trend can be, and has been, impacted somewhat by significant governmental funding initiatives and significant industrial projects.

Historically, inventories have increased through the year to meet the expected demand for higher deliveries in the third and fourth quarters of the fiscal year. This seasonal sales trend also leads accounts receivable to be at their highest level at year-end.

## SELECTED ANNUAL INFORMATION

<i>(in thousands, except per share amounts)</i>	2017	2016	2015
Revenues	\$ 2,350,162	\$ 1,912,040	\$ 1,846,723
Net earnings	\$ 175,970	\$ 155,748	\$ 145,666
Earnings per share			
- Basic	\$ 2.22	\$ 1.99	\$ 1.88
- Diluted	\$ 2.20	\$ 1.98	\$ 1.86
Dividends declared per share	\$ 0.76	\$ 0.72	\$ 0.68
Total assets	\$ 2,857,909	\$ 1,394,212	\$ 1,276,077
Total long-term debt	\$ 895,747	\$ 152,528	\$ 153,769
Weighted average common shares outstanding, basic (millions)	79.9	78.7	77.7

Revenues grew 23% in 2017 inclusive of the two months of operations at Toromont QM which generated revenues of \$242.6 million. For the legacy businesses, revenues grew 10% on good sales execution in the Equipment Group and CIMCO, underpinned by continued product support growth. In 2016, revenues grew 4% mainly through strong performance at CIMCO, as the Equipment Group grew modestly on product support growth which served to offset the impact of challenging equipment market conditions.

Net earnings increased 13% in 2017, reflecting higher revenues and a relatively lower expense ratio, in addition to the incremental impact of the acquisition. Lower margins, especially in the

Equipment Group, diluted earnings. Selling and administrative expenses included acquisition-related expenses and the impact of higher DSU mark-to-market expenses on the higher average share price following the announcement of the acquisition. Higher interest expense resulting from increased debt levels to partially fund the acquisition, also dampened net earnings. In 2016, net earnings increased 7% on higher revenues and slightly improved gross margins, partially offset by a higher selling and administrative expense ratio. A one-time pre-tax gain of \$4.9 million on the sale of internally-developed software recorded in 2016 also lifted earnings.

Earnings per share (“EPS”) have generally followed earnings with basic EPS increasing 12% in 2017 and 6% in 2016.

Dividends have generally increased in proportion to trailing earnings growth. The quarterly dividend rate was increased in 2015 by 13% to \$0.17 per share, in 2016 by 6% to \$0.18 per share, in 2017 by 6% to \$0.19 per share and in 2018 by 21% to \$0.23 per share. The Company has paid dividends every year since 1968.

Total assets more than doubled in 2017 (up 105%) reflecting the acquisition and growth in the Company’s operations and supports the higher revenues and earnings. Total assets increased 9% in 2016.

Long-term debt increased in 2017 to partially fund the acquisition. In 2016, long-term debt had decreased relative to 2015 mainly due to principal repayments on the senior debenture due in March 2019, net of the amortization of debt issuance costs. Net debt to total capitalization at December 31, 2017, was 40% compared to -4% at December 31, 2016 (cash exceeded total debt).

## **RISKS AND RISK MANAGEMENT**

In the normal course of business, Toromont is exposed to risks that may potentially impact its financial results in any or all of its business segments. The Company and each operating segment employ risk management strategies with a view to mitigating these risks on a cost-effective basis.

### Acquisition and integration of the Hewitt operations

Risks and uncertainties exist related to the acquisition of the Hewitt operations including but not limited to: changes in consumer and business confidence as a result of the change in ownership; the potential for liabilities assumed in the acquisition to exceed our estimates or for material undiscovered liabilities in the Hewitt Business; the potential for third parties to terminate or alter their agreements or relationships with Toromont as a result of the Acquisition.

The anticipated benefits and synergies from acquiring Hewitt will depend in part on whether the operations, systems, management and cultures of Hewitt and Toromont can be integrated in an efficient and effective manner. While certain operational and strategic decisions with respect to the combined organization have been made, other decisions remain and some may not have been identified. These decisions and the integration of Hewitt with the existing Toromont businesses will present significant challenges to management. The integration process may lead to greater than expected operating costs, customer loss and business disruption (including, without limitation, difficulties in maintaining relationships with employees, customers or

suppliers) for Toromont or the combined organization that may affect the ability of the combined organization to realize the anticipated benefits of the combination or may otherwise materially and adversely affect Toromont's business, results of operations or financial condition.

### Business Cycle

Expenditures on capital goods have historically been cyclical, reflecting a variety of factors including interest rates, foreign exchange rates, consumer and business confidence, commodity prices, corporate profits, credit conditions and the availability of capital to finance purchases. Toromont's customers are typically affected, to varying degrees, by these factors and trends in the general business cycle within their respective markets. As a result, Toromont's financial performance is affected by the impact of such business cycles on the Company's customer base.

Commodity prices, and, in particular, changes in the view on long-term trends, affects demand for the Company's products and services in the Equipment Group. Commodity price movements in base and precious metals sectors in particular can have an impact on customers' demands for equipment and service. With lower commodity prices, demand is reduced as development of new projects is often stopped and existing projects can be curtailed, both leading to less demand for heavy equipment.

The business of the Company is diversified across a wide range of industry market segments, serving to temper the effects of business cycles on consolidated results. Continued diversification strategies such as expanding the Company's customer base, broadening product offerings and geographic diversification are designed to moderate business cycle impacts. The Company has focused on the sale of specialized equipment and ongoing support through parts distribution and skilled service. Product support growth has been, and will continue to be, fundamental to the mitigation of downturns in the business cycle. The product support business contributes significantly higher profit margins and is typically subject to less volatility than equipment supply activities.

### Product and Supply

The Equipment Group purchases most of its equipment inventories and parts from Caterpillar under a dealership agreement that dates back to 1993. As is customary in distribution arrangements of this type, the agreement with Caterpillar can be terminated by either party upon 90 days' notice. In the event Caterpillar terminates, it must repurchase substantially all inventories of new equipment and parts at cost. Toromont has maintained an excellent relationship with Caterpillar for 25 years and management expects this will continue going forward.

Toromont is dependent on the continued market acceptance of Caterpillar's products. It is believed that Caterpillar has a solid reputation as a high-quality manufacturer, with excellent brand recognition and customer support as well as leading market shares in many of the markets it serves. However, there can be no assurance that Caterpillar will be able to maintain its reputation and market position in the future. Any resulting decrease in the demand for Caterpillar products could have a material adverse impact on the Company's business, results of operations and future prospects.

Toromont is also dependent on Caterpillar for timely supply of equipment and parts. From time to time during periods of intense demand, Caterpillar may find it necessary to allocate its supply

of particular products among its dealers. Such allocations of supply have not, in the past, proven to be a significant impediment in the conduct of business. However, there can be no assurance that Caterpillar will continue to supply its products in the quantities and timeframes required by customers.

### Competition

The Company competes with a large number of international, national, regional and local suppliers in each of its markets. Although price competition can be strong, there are a number of factors that have enhanced the Company's ability to compete throughout its market areas including the range and quality of products and services, ability to meet sophisticated customer requirements, distribution capabilities including number and proximity of locations, financing offered by Caterpillar Finance, e-commerce solutions, reputation and financial strength.

Increased competitive pressures or the inability of the Company to maintain the factors that have enhanced its competitive position to date could adversely affect the Company's business, results of operations or financial condition.

The Company relies on the skills and availability of trained and experienced tradesmen and technicians in order to provide efficient and appropriate services to customers. Hiring and retaining such individuals is critical to the success of these businesses. Demographic trends are reducing the number of individuals entering the trades, making access to skilled individuals more difficult. The Company has several remote locations which make attracting and retaining skilled individuals more difficult.

### Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist of cash equivalents, accounts receivable and derivative financial instruments. The carrying amount of assets included on the balance sheet represents the maximum credit exposure.

When the Company has cash on hand it may be invested in short-term instruments, such as money-market deposits. The Company has deposited cash with reputable financial institutions, from which management believes the risk of loss to be remote.

The Company has accounts receivable from a large diversified customer base, and is not dependent on any single customer or industry. The Company has accounts receivable from customers engaged in various industries including construction, mining, food and beverage, and governmental agencies. Management does not believe that any single customer represents significant credit risk. These customers are based predominately in Canada.

The credit risk associated with derivative financial instruments arises from the possibility that the counterparties may default on their obligations. In order to minimize this risk, the Company enters into derivative transactions only with highly rated financial institutions.

### Warranties and Maintenance Contracts

Warranties are provided for most of the equipment sold, typically for a one-year period following sale. The warranty claim risk is generally shared jointly with the equipment manufacturer. Accordingly, liability is generally limited to the service component of the warranty claim, while the manufacturer is responsible for providing the required parts.

The Company also enters into long-term maintenance and repair contracts, whereby it is obligated to maintain equipment for its customers. The length of these contracts varies generally from two to five years. The contracts are typically fixed price on either machine hours or cost per hour, with provisions for inflationary and exchange adjustments. Due to the long-term nature of these contracts, there is a risk that maintenance costs may exceed the estimate, thereby resulting in a loss on the contract. These contracts are closely monitored for early warning signs of cost overruns. In addition, the manufacturer may, in certain circumstances, share in the cost overruns if profitability falls below a certain threshold.

### Foreign Exchange

The Company transacts business in multiple currencies, the most significant of which are the Canadian dollar and the US dollar. As a result, the Company has foreign currency exposure with respect to items denominated in foreign currencies.

The rate of exchange between the Canadian and US dollar has an impact on revenue trends. The Canadian dollar averaged US\$0.77 in 2017 compared to US\$0.75 in 2016, a 2% increase. As substantially all of the equipment and parts sold in the Equipment Group are sourced in US dollars, and Canadian dollar sales prices generally reflect changes in the rate of exchange, a stronger Canadian dollar can adversely affect revenues. The impact is not readily estimable as it is largely dependent on when customers order the equipment versus when it was sold. Bookings in a given period would more closely follow period-over-period changes in exchange rates. Sales of parts come from inventories maintained to service customer requirements. As a result, constant parts replenishment means that there is a lagging impact of changes in exchange rates. In CIMCO, sales are largely affected by the same factors. In addition, revenues from CIMCO's US subsidiary reflect changes in exchange rates on the translation of results, although this is not significant.

Foreign exchange contracts reduce volatility by fixing landed costs related to specific customer orders and establishing a level of price stability for high-volume goods such as spare parts. The Company does not enter into foreign exchange forward contracts for speculative purposes. The gains and losses on the foreign exchange forward contracts designated as cash flow hedges are intended to offset the translation losses and gains on the hedged foreign currency transactions when they occur. As a result, the foreign exchange impact on earnings with respect to transactional activity is not significant.

### Interest Rate

The Company minimizes its interest rate risk by managing its portfolio of floating-and fixed-rate debt, as well as managing the term to maturity.

At December 31, 2017, the Company's debt portfolio included \$653.0 million in fixed-rate debt (72% of total debt outstanding) and a \$750.0 million floating-rate credit facility, of which \$250 million was drawn (28% of total debt outstanding).

Fixed-rate debt amortizes or matures between 2018 and 2027. Fixed-rate debt exposes the Company to future interest rate movements upon refinancing the debt at maturity. Further, the fair value of the Company's fixed-rate debt obligations may be negatively affected by declines in interest rates, thereby exposing the Company to potential losses on early settlements or refinancing.

Floating-rate debt exposes the Company to fluctuations in short-term interest rates by causing related interest payments and finance expense to vary.

The Company does not intend to settle or refinance any existing fixed-rate debt before maturity.

### Financing Arrangements

The Company requires capital to finance its growth and to refinance its outstanding debt obligations as they come due for repayment. If the cash generated from the Company's business, together with the credit available under existing bank facilities, is not sufficient to fund future capital requirements, the Company will require additional debt or equity financing in the capital markets. The Company's ability to access capital markets, on terms that are acceptable, will be dependent upon prevailing market conditions, as well as the Company's future financial condition. Further, the Company's ability to increase its debt financing may be limited by its financial covenants or its credit rating objectives. The Company maintains a conservative leverage structure and although it does not anticipate difficulties, there can be no assurance that capital will be available on suitable terms and conditions, or that borrowing costs and credit ratings will not be adversely affected.

### Environmental Regulation

Toromont's customers are subject to significant and ever-increasing environmental legislation and regulation. This legislation can impact Toromont in two ways. First, it may increase the technical difficulty in meeting environmental requirements in product design, which could increase the cost of these businesses' products. Second, it may result in a reduction in activity by Toromont's customers in environmentally sensitive areas, in turn reducing the sales opportunities available to Toromont.

Toromont is also subject to a broad range of environmental laws and regulations. These may, in certain circumstances, impose strict liability for environmental contamination, which may render Toromont liable for remediation costs, natural resource damages and other damages as a result of conduct that was lawful at the time it occurred or the conduct of, or conditions caused by, prior owners, operators or other third parties. In addition, where contamination may be present, it is not uncommon for neighbouring land owners and other third parties to file claims for personal injury, property damage and recovery of response costs. Remediation costs and other damages arising as a result of environmental laws and regulations, and costs associated with new information, changes in existing environmental laws and regulations or the adoption of new environmental laws and regulations could be substantial and could negatively impact Toromont's business, results of operations or financial condition.

## **SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES**

The Company's significant accounting policies are described in note 1 of the notes to the consolidated financial statements.

The preparation of the Company's consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

In making estimates and judgments, management relies on external information and observable conditions where possible, supplemented by internal analysis as required. Management reviews its estimates and judgments on an ongoing basis.

In the process of applying the Company's accounting policies, management has made the following judgments, estimates and assumptions which have the most significant effect on the amounts recognized in the consolidated financial statements. The critical accounting policies and estimates described below affect the operating segments similarly, and therefore are not discussed on a segmented basis.

### **Acquisitions**

In a business combination, the Company may acquire certain assets and assume certain liabilities of an acquired entity. The estimate of fair values for these transactions involves judgment to determine the fair values assigned to the tangible and intangible assets (i.e., backlog, client relationships, and distribution networks) acquired and the liabilities assumed on the acquisition. Determining fair value involves a variety of assumptions, including revenue growth rates, expected operating income, and discount rates. During a measurement period, not to exceed one year, adjustments of the initial estimates may be required to finalize the fair value of assets acquired and liabilities assumed. After the measurement period, a revision of fair value may impact the Company's net income.

### **Property, Plant and Equipment**

Depreciation is calculated based on the estimated useful lives of the assets and estimated residual values. Depreciation expense is sensitive to the estimated service lives and residual values determined for each type of asset. Actual lives and residual values may vary depending on a number of factors including technological innovation, product life cycles and physical condition of the asset, prospective use, and maintenance programs.

### **Impairment of Non-financial Assets**

Judgment is used in identifying an appropriate discount rate and growth rate for the calculations required in assessing potential impairment of non-financial assets. Judgment is also used in identifying the cash generating units ("CGUs") to which the intangible assets should be allocated, and the CGU or group of CGUs at which goodwill is monitored for internal management purposes. The impairment calculations require the use of estimates related to the future operating results and cash generating ability of the assets. The key assumptions used to determine the recoverable amount for the different groups of CGUs, including a sensitivity

analysis, are disclosed and further explained in note 8 of the notes to the consolidated financial statements.

### **Income Taxes**

Estimates and judgments are made for uncertainties which exist with respect to the interpretation of complex tax regulations, changes in tax laws, and the amount and timing of future taxable income.

### **Revenue Recognition**

Recording revenues from the assembly and manufacture of equipment using the percentage-of-completion method requires management to make a number of estimates and assumptions about the expected profitability of the contract, the estimated degree of completion based on cost progression and other detailed factors. These factors are routinely reviewed as part of the project management process.

The Company also generates revenue from long-term maintenance and repair contracts whereby it is obligated to maintain equipment for its customers. The contracts are typically fixed price on either machine hours or cost per hour, with provisions for inflationary and exchange adjustments. Revenue is recognized using the percentage-of-completion method based on work completed. This method requires management to make a number of estimates and assumptions surrounding machine usage, machine performance, future parts and labour pricing, manufacturers' warranty coverage and other detailed factors. These factors are routinely reviewed as part of the contract management process.

### **Inventories**

Management is required to make an assessment of the net realizable value of inventory at each reporting period. These estimates are determined on the basis of age, stock levels, current market prices, current economic trends and past experience in the measurement of net realizable value.

### **Allowance for Doubtful Accounts**

The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar assets in respect of losses that may have been incurred but not yet specifically identified. By their nature, these are estimates based on management's judgment and historical experience.

### **Share-based Compensation**

The option pricing model used to determine the fair value of share-based payments requires various estimates relating to volatility, interest rates, dividend yields and expected life of the options granted. Fair value inputs are subject to market factors as well as internal estimates. The Company considers historic trends together with any new information to determine the best estimate of fair value at the date of grant. Separate from the fair value calculation, the Company is required to estimate the expected forfeiture rate of equity-settled share-based payments.

## **Post-Employment Benefit Plans**

The Company has defined benefit pension plans and other post-employment benefit plans that provide certain benefits to its employees. Actuarial valuations of these plans are based on assumptions which include discount rates, retail price inflation, mortality rates, employee turnover and salary escalation rates. Judgment is exercised in setting these assumptions. These assumptions impact the measurement of the net employee benefit obligation, funding levels, the net benefit cost and the actuarial gains and losses recognized in other comprehensive income.

## **Changes in Accounting Policies**

Effective January 1, 2017, The Company adopted the amendments to IAS 7 – Statement of Cash Flows. The amendments introduce new requirements to disclose changes in liabilities arising from financing activities, included changes arising from cash flows and non-cash flows. The required disclosures have been added to note 21 of the notes to the consolidated financial statements.

## **Pending Accounting Changes**

A number of new standards and amendments to standards have been issued but were not yet effective for the financial year ending December 31, 2017, and accordingly, have not been applied in preparing these consolidated financial statements. The effect of future accounting pronouncements and effective dates are discussed in note 1 of the notes to the consolidated financial statements.

## **CONTROLS AND PROCEDURES**

### Disclosure Controls and Procedures

Management, under the supervision of the President and Chief Executive Officer (“CEO”) and Executive Vice President and Chief Financial Officer (“CFO”), is responsible for establishing and maintaining disclosure controls and procedures, as defined in National Instrument 52-109 – *Certification of Disclosure in Issuers’ Annual and Interim Filings*, and have designed such disclosure controls and procedures, or have caused it to be designed under their supervision, to provide reasonable assurance that material information with respect to Toromont is made known to them.

The CEO and the CFO, together with other members of management, have evaluated the effectiveness of the Company’s disclosure controls and procedures. The CEO and CFO have limited the scope of their design and evaluation of the Company’s disclosure controls and procedures to exclude the disclosure controls and procedures of Hewitt’s operations, which were acquired on October 27, 2017. Hewitt’s contribution to the overall consolidated financial statements of Toromont for the year ended December 31, 2017 was approximately 10% of consolidated revenues and 4% of consolidated net income. The design of Hewitt’s disclosure controls and procedures will be completed for the fourth quarter of fiscal 2018.

Based on that evaluation, which excluded Hewitt’s disclosure controls and procedures, the CEO and CFO conclude that the Company’s disclosure controls and procedures were effective as at December 31, 2017.

## Internal Control over Financial Reporting

Management, under the supervision of the CEO and CFO, is responsible for establishing and maintaining adequate internal control over financial reporting, as defined by National Instrument 52-109 – *Certification of Disclosure in Issuers' Annual and Interim Filings*, and have designed such internal control over financial reporting, or caused it to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the consolidated financial statements in accordance with IFRS.

The CEO and the CFO, together with other members of management, have evaluated the effectiveness of the Company's internal control over financial reporting as at December 31, 2017, using the criteria set forth in *Internal Control - Integrated Framework* (2013 edition) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

The CEO and CFO have limited the scope of their design and evaluation of the Company's internal control over financial reporting to exclude the internal control over financial reporting of the Hewitt operations, which were acquired on October 27, 2017.

Based on that evaluation, which excluded Hewitt's internal control over financial reporting, the CEO and CFO concluded that the Company's internal control over financial reporting was effective as at December 31, 2017.

There have been no changes in the design of the Company's internal control over financial reporting during 2017 that would materially affect, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis. Also, a projection of the evaluation of the effectiveness of internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to the financial statement preparation and presentation. Internal controls over financial reporting may not prevent all errors and fraud. A control system, no matter how well conceived or operated, can only provide reasonable, not absolute, assurance that the objectives of the control system are met.

## ADDITIONAL GAAP MEASURES

IFRS mandates certain minimum line items for financial statements and also requires presentation of additional line items, headings and subtotals when such presentation is relevant to an understanding of the Company's financial position or performance. IFRS also requires the notes to the financial statements to provide information that is not presented elsewhere in the financial statements, but is relevant to understanding them. Such measures outside of the minimum mandated line items are considered additional GAAP measures. The Company's consolidated financial statements and notes thereto include certain additional GAAP measures where management considers such information to be useful to the understanding of the Company's results.

### *Gross Profit*

Gross Profit is defined as total revenues less cost of goods sold.

### *Operating Income*

Operating income is defined as net earnings before interest expense, interest and investment income and income taxes and is used by management to assess and evaluate the financial performance of its operating segments. Financing and related interest charges cannot be attributed to business segments on a meaningful basis that is comparable to other companies. Business segments do not correspond to income tax jurisdictions, and it is believed that the allocation of income taxes distorts the historical comparability of the performance of the business segments.

(\$ thousands)	Three months ended December 31		Years ended December 31	
	2017	2016	2017	2016
Net earnings	\$ 59,136	\$ 45,529	\$ 175,970	\$ 155,748
plus: Interest expense	6,788	1,853	12,277	7,242
less: Interest and investment income	(1,637)	(1,377)	(4,659)	(4,006)
plus: Income taxes	22,294	16,883	65,994	57,579
<b>Operating income</b>	<b>\$ 86,581</b>	<b>\$ 62,888</b>	<b>\$ 249,582</b>	<b>\$ 216,563</b>

### *Net Debt to Total Capitalization and Equity*

Net debt to total capitalization and equity are calculated as net debt divided by total capitalization and shareholders' equity, respectively, as defined below, and are used by management as measures of the Company's financial leverage.

Net debt is calculated as long-term debt plus current portion of long-term debt less cash. Total capitalization is calculated as shareholders' equity plus net debt.

The calculations are as follows:

<i>(\$ thousands)</i>	<b>2017</b>	2016
Long-term debt	\$ 893,806	\$ 150,717
Current portion of long-term debt	1,941	1,811
<i>less: Cash</i>	160,507	188,735
<b>Net debt</b>	<b>\$ 735,240</b>	<b>\$ (36,207)</b>
Shareholders' equity	\$ 1,124,727	\$ 885,432
<b>Total capitalization</b>	<b>\$ 1,859,967</b>	<b>\$ 849,225</b>
<b>Net debt to total capitalization</b>	<b>40%</b>	<b>-4%</b>
<b>Net debt to equity</b>	<b>0.65:1</b>	<b>-0.04:1</b>

For the year ended December 31, 2016, cash exceeded total debt and effectively resulted in negative net debt to total capitalization and equity ratios, as illustrated above.

## NON-GAAP MEASURES

Management believes that providing certain non-GAAP measures provides users of the Company's consolidated financial statements with important information regarding the operational performance and related trends of the Company's business. By considering these measures in combination with the comparable IFRS measures set out below, management believes that users are provided a better overall understanding of the Company's business and its financial performance during the relevant period than if they simply considered the IFRS measures alone.

The non-GAAP measures used by management do not have any standardized meaning prescribed by IFRS and are therefore unlikely to be comparable to similar measures presented by other issuers. Accordingly, these measures should not be considered as a substitute or alternative for net income or cash flow, in each case as determined in accordance with IFRS.

### *Working Capital*

Working capital is defined as total current assets less total current liabilities. Management views working capital as a measure for assessing overall liquidity.

<i>(\$ thousands)</i>	<b>2017</b>	2016
Total current assets	\$ 1,477,665	\$ 891,616
<i>less: Total current liabilities</i>	699,291	316,234
<b>Working capital</b>	<b>\$ 778,374</b>	<b>\$ 575,382</b>

### Non-Cash Working Capital

Non-cash working capital is defined as total current assets (excluding cash) less total current liabilities (excluding current portion of long-term debt).

(\$ thousands)	2017	2016
Total current assets	\$ 1,477,665	\$ 891,616
less: Cash	160,507	188,735
	\$ 1,317,158	\$ 702,881
Total current liabilities	\$ 699,291	\$ 316,234
less: Current portion of long-term debt	1,941	1,811
	\$ 697,350	\$ 314,423
<b>Non-cash working capital</b>	<b>\$ 619,808</b>	<b>\$ 388,458</b>

### Market Capitalization & Total Enterprise Value

Market capitalization represents the total market value of the Company's equity. It is calculated by multiplying the market price of the Company's share by the total outstanding shares.

Total enterprise value represents the total value of the Company and is often used as a more comprehensive alternative to market capitalization. It is calculated by adding net debt (defined above) to market capitalization.

The calculations are as follows:

(\$ thousands, except for share price)	2017	2016
Outstanding common shares, December 31	80,950	78,398
x Ending share price, December 31	\$ 55.10	\$ 42.35
<b>Market capitalization</b>	<b>\$ 4,460,335</b>	<b>\$ 3,320,175</b>
Long-term debt	\$ 893,806	\$ 150,717
Current portion of long-term debt	1,941	1,811
less: Cash	160,507	188,735
<b>Net debt</b>	<b>\$ 735,240</b>	<b>\$ (36,207)</b>
<b>Total enterprise value</b>	<b>\$ 5,195,575</b>	<b>\$ 3,283,968</b>

### Key Performance Indicators ("KPIs")

Management uses key performance indicators to consistently measure performance against the Company's priorities across the organization. The Company's KPIs include gross profit margin, operating margin, order bookings and backlogs, return on capital employed and return on equity. Although some of these KPIs are expressed as ratios, they are non-GAAP financial measures that do not have a standardized meaning under IFRS and may not be comparable to similar measures used by other issuers.

### Gross Profit Margin

This measure is defined as gross profit (defined above) divided by total revenues.

### Operating Income Margin

This measure is defined as operating income (defined above) divided by total revenues.

### Order Bookings and Backlogs

The Company's order bookings represent equipment unit orders that management believes are firm. Backlogs are defined as the retail value of equipment unit ordered by customers for future deliveries. Management uses order backlog as a measure of projecting future equipment deliveries. There are no directly comparable IFRS measures for order bookings or backlog.

### Return on Capital Employed ("ROCE")

ROCE is utilized to assess both current operating performance and prospective investments. The numerator used for the calculation is income before income taxes, interest expense and interest income (excluding interest on rental conversions). The denominator in the calculation is the monthly average capital employed, which is defined as net debt plus shareholders' equity or total capitalization.

(\$ thousands)	2017	2016
Net earnings	\$ 175,970	\$ 155,748
<i>plus:</i> Interest expense	12,277	7,242
<i>less:</i> Interest and investment income	(4,659)	(4,006)
<i>plus:</i> Interest income - rental conversions (see note 14)	2,308	2,811
<i>plus:</i> Income taxes	65,994	57,579
	\$ 251,890	\$ 219,374
Average capital employed	\$ 1,171,449	\$ 894,765
<b>Return on capital employed</b>	<b>21.5%</b>	24.5%

### Return on Equity ("ROE")

ROE is monitored to assess the profitability of the consolidated Company and is calculated by dividing net earnings by opening shareholders' equity (adjusted for shares issued and redeemed during the year).

(\$ thousands)	2017	2016
Net earnings	\$ 175,970	\$ 155,748
Opening shareholders' equity (net of adjustments)	\$ 909,715	\$ 778,896
<b>Return on equity</b>	<b>19.3%</b>	20.0%