# Q3 2008

For the three months ended Sept 30, 2008

CANFOR CORPORATION 2008 THIRD QUARTER INTERIM REPORT

## To Our Shareholders

Canfor Corporation reported a net loss of $94.2 million ($0.66 per share) for the third quarter of 2008, compared to net income of $64.2 million ($0.45 per share) for the second quarter of 2008 and a net loss of $42.1 million ($0.30 per share) for the third quarter of 2007. For the nine months ended September 30, 2008, the Company's net loss was $115.4 million ($0.81 per share), compared to a net loss of $123.6 million ($0.87 per share) reported for the comparable period in 2007.

The net loss for the third quarter of 2008 included the following significant items, which together had a negative impact on net income of $89.6 million ($0.63 per share):

- An asset impairment charge of $56.9 million ($0.40 per share), related to the Company's investments in Howe Sound Pulp and Paper Limited Partnership. The impairment reflects the continuing deterioration of B.C. Coastal pulp, paper and fibre market conditions.
- Losses recorded on derivative financial instruments of $21.4 million ($0.15 per share), reflecting a sharp decline in energy prices and a weaker Canadian dollar in the third quarter. Year-to-date, the loss related to these contracts was $4.2 million.
- A foreign exchange translation loss on the Company's US-dollar denominated debt, net of investments, of $11.3 million ($0.08 per share), as a result of the weaker Canadian dollar.

After taking account of these and several smaller one-time items which affected comparability with prior periods, the Company reported an adjusted net loss for the third quarter of 2008 of $3.5 million ($0.02 per share), compared to similarly adjusted net losses of $20.8 million ($0.15 per share) for the second quarter of 2008 and $45.9 million ($0.33 per share) for the third quarter of 2007.

The improvement in adjusted earnings reflected the Company's continued progress in the reduction of its operating costs in the quarter, despite challenges presented by significant production curtailments and increased transportation costs. Higher lumber prices, the weaker Canadian dollar and the absence of Canfor Pulp Limited Partnership's second quarter scheduled maintenance outages were also significant contributing factors to the improved results.

Canfor continued to face major challenges on a number of fronts in the third quarter of 2008. U.S. housing starts, already at historically-low levels, fell even further in September, as a result of the upheaval in global financial and credit markets and heightened concerns about the U.S. economy. Prices for lumber and oriented strand board (OSB) products, which had edged up over the summer months, largely as a result of tighter supply, dropped off sharply towards the quarter end, erasing earlier gains. Pulp markets weakened in the third quarter as a result of falling global demand, and prices came under considerable pressure late in the quarter. Prices for all wood and pulp products continued to deteriorate after quarter end. Reflecting the very tough market conditions, the Company made the decision in early October to indefinitely close its Tackama plywood plant in Fort Nelson, British Columbia.

Canadian lumber producers continued to be subject to a 15% export tax on shipments to the U.S. in the third quarter. On a more positive note, however, the Canadian dollar weakened relative to its U.S. counterpart through the third quarter, averaging US$0.960 compared to US$0.990 in the second quarter, which boosted Canadian dollar sales values.

The Company expected conditions for all of its products to be extremely challenging through the balance of 2008 and in 2009 in view of the current financial and credit market turmoil and weak U.S. economic outlook.

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|---|---|
| **Peter J.G. Bentley** | **James F. Shepard** |
| **Chairman** | **President and Chief Executive Officer** |

**Canfor Corporation**
**Third Quarter 2008**
**Management's Discussion and Analysis**

This interim Management's Discussion and Analysis (MD&A) provides a review of Canfor's financial performance for the quarter ended September 30, 2008 relative to the quarters ended June 30, 2008 and September 30, 2007, and the financial condition of the Company. It should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes for the quarters ended September 30, 2008 and 2007, as well as the 2007 annual MD&A and audited consolidated financial statements and notes thereto, which are included in Canfor's Annual Report for the year ended December 31, 2007 (available at www.canfor.com).

Throughout this discussion, reference is made to EBITDA (calculated as operating income before amortization), which Canfor considers to be an important indicator for identifying trends in the performance of each of its operating segments and the Company's ability to generate funds to meet its debt repayment and capital expenditure requirements. EBITDA is not a generally accepted earnings measure and should not be considered as an alternative to net income or cash flows as determined in accordance with Canadian generally accepted accounting principles (GAAP). As there is no standardized method of calculating EBITDA, Canfor's EBITDA may not be directly comparable with similarly titled measures used by other companies. A reconciliation of EBITDA to net income reported in accordance with GAAP is included in this MD&A.

Factors that could impact future operations are also discussed. These factors may be influenced by known and unknown risks and uncertainties that could cause the actual results to be materially different from those stated in this discussion. Factors that could have a material impact on any future oriented statements made herein include, but are not limited to: general economic, market and business conditions; product selling prices; raw material and operating costs; foreign exchange rates; changes in law and public policy; the outcome of trade disputes; and opportunities available to or pursued by Canfor.

Certain prior period comparative information throughout this report has been restated for consistency with the presentation in the current period. All financial references are in millions of Canadian dollars unless otherwise noted. The information in this report is as at October 29, 2008.

## THIRD QUARTER 2008 EARNINGS OVERVIEW

Selected Financial Information and Statistics

| (millions of dollars, except for per share amounts) | Q3 2008 | Q2 2008 [5] | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| Sales | **$ 668.0** | $ 706.4 | **$ 2,022.9** | $ 837.4 | $ 2,564.6 |
| EBITDA[1] | **$ 55.1** | $ 62.3 | **$ 43.3** | $ (6.5) | $ (11.4) |
| Operating income (loss) [1] | **$ 12.8** | $ 20.8 | **$ (83.9)** | $ (52.1) | $ (148.3) |
| Foreign exchange gain (loss) on long-term debt and investments, net | **$ (16.2)** | $ (0.1) | **$ (28.3)** | $ 9.5 | $ 20.3 |
| Gain (loss) on derivative financial instruments [2] | **$ (38.8)** | $ 26.0 | **$ (6.8)** | $ 8.9 | $ 9.8 |
| Asset impairments | **$ (70.0)** | $ - | **$ (70.0)** | $ (7.0) | $ (12.0) |
| Prince George Pulp & Paper mill fire, net | **$ -** | $ - | **$ 8.5** | $ - | $ - |
| North Central Plywoods mill fire, net | **$ -** | $ 57.9 | **$ 57.9** | $ - | $ - |
| Net income (loss) [1] | **$ (94.2)** | $ 64.2 | **$ (115.4)** | $ (42.1) | $ (123.6) |
| Net income (loss) per share, basic and diluted [1] | **$ (0.66)** | $ 0.45 | **$ (0.81)** | $ (0.30) | $ (0.87) |
| Average exchange rate (US$/CDN$) [3] | **$ 0.960** | $ 0.990 | **$ 0.982** | $ 0.957 | $ 0.905 |
| U.S. housing starts (million units SAAR) [4] | **0.879** | 1.025 | **0.986** | 1.298 | 1.404 |

[1] Results for the first nine months of 2008 reflect the Company's prospective adoption on January 1, 2008 of CICA Handbook Section 3031, *Inventories*, which requires all inventories, including logs, to be valued at the lower of cost or net realizable value. Details of related write-downs and reversals are contained in the following pages. The adjustments affect comparability with prior periods.
[2] Includes gains (losses) from hedging of natural gas, diesel, foreign exchange rates and lumber prices (see "Non-Segmented Items" section for more details).
[3] Source – Bank of Canada (average noon rate for the period)
[4] Source – U.S. Census Bureau, seasonally adjusted annual rate (SAAR)
[5] Certain amounts in prior periods have been reclassified to conform to the presentation in the current period.

## Overview

### *Net Income (Loss)*

The Company recorded a net loss of $94.2 million ($0.66 per share) for the third quarter of 2008, a decrease of $158.4 million compared to a net profit of $64.2 million ($0.45 per share) reported for the second quarter of 2008, and $52.1 million ($0.36 per share) higher than the net loss of $42.1 million reported for the third quarter of 2007. After adjusting for significant items affecting comparability with prior periods, the Company's adjusted net loss was $3.5 million ($0.02 per share) for the third quarter of 2008, compared to a similarly adjusted loss of $20.8 million ($0.15 per share) for the second quarter of 2008, and an adjusted loss of $45.9 million ($0.33 per share) for the third quarter of 2007.

The quarterly results in 2008 reflect the Company's prospective adoption of CICA Handbook Section 3031, *Inventories,* on January 1, 2008, which requires inventories, including logs, to be valued at the lower of cost or net realizable value (previously, the Company valued logs at the higher of net realizable value and replacement cost, if lower than average cost). In the first quarter, there was a seasonal build of log inventories which was then followed in the second quarter by a reduction of log inventories during spring break up. At the end of the third quarter, log inventory levels and write-downs from cost to net realizable value were similar to those at the end of the second quarter. As a result, the adoption of the new accounting standard had only a minor positive impact on the third quarter's operating income and net income ($3.9 million and $2.5 million ($0.02 per share), respectively), in contrast to the second quarter, when the Company added $72.4 million to operating income, and $47.8 million ($0.34 per share) to net income. For the nine months ended September 30, 2008, the new accounting standard has resulted in an increase in operating income and net income of $34.3 million and $21.3 million ($0.15 per share), respectively.

Analysis of Specific Items Affecting Comparability of Net Income (Loss)

| After-tax impact, net of non-controlling interests (millions of dollars, except per share amounts) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| **Net income (loss), as reported** | **$ (94.2)** | $ 64.2 | **$ (115.4)** | $ (42.1) | $ (123.6) |
| (Gain) loss on derivative financial instruments | **$ 21.4** | $ (14.5) | **$ 4.2** | $ (6.9) | $ (8.1) |
| New inventory accounting standard | **$ (2.5)** | $ (47.8) | **$ (21.3)** | $ - | $ - |
| Foreign exchange (gain) loss on long-term debt and investments, net | **$ 11.3** | $ - | **$ 20.0** | $ (5.1) | $ (10.0) |
| Prince George Pulp & Paper mill fire, net | **$ -** | $ - | **$ (3.6)** | $ - | $ - |
| North Central Plywoods mill fire, net | **$ -** | $ (45.0) | **$ (45.0)** | $ - | $ - |
| Restructuring, mill closure and severance costs | **$ 3.6** | $ 22.3 | **$ 28.5** | $ 7.3 | $ 13.1 |
| Corporate income tax rate reductions | **$ -** | $ - | **$ (9.1)** | $ (0.9) | $ (1.9) |
| Asset impairments | **$ 56.9** | $ - | **$ 56.9** | $ 6.0 | $ 10.1 |
| Other items | **$ -** | $ - | **$ -** | $ (4.2) | $ (9.0) |
| Net impact of above items | **$ 90.7** | $ (85.0) | **$ 30.6** | $ (3.8) | $ (5.8) |
| **Net income (loss), as adjusted** | **$ (3.5)** | **$ (20.8)** | **$ (84.8)** | **$ (45.9)** | **$ (129.4)** |
| **Net income (loss) per share, as reported** | **$ (0.66)** | **$ 0.45** | **$ (0.81)** | **$ (0.30)** | **$ (0.87)** |
| Net impact of above items per share | **$ 0.64** | $ (0.60) | **$ 0.22** | $ (0.03) | $ (0.04) |
| **Net income (loss) per share, as adjusted** | **$ (0.02)** | **$ (0.15)** | **$ (0.59)** | **$ (0.33)** | **$ (0.91)** |

EBITDA

The following table reconciles the Company's net income (loss), as reported in accordance with GAAP, to EBITDA:

| (millions of dollars) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| **Net income (loss), as reported** | **$ (94.2)** | $ 64.2 | **$ (115.4)** | $ (42.1) | $ (123.6) |
| Add (subtract): | | | | | |
| Non-controlling interests | **$ 5.4** | $ 9.2 | **$ 36.6** | $ 16.9 | $ 59.3 |
| Income tax expense (recovery) | **$ (30.0)** | $ 24.0 | **$ (61.7)** | $ (27.2) | $ (78.8) |
| Other (income) expense | **$ (0.1)** | $ 1.5 | **$ 0.2** | $ 9.3 | $ 7.8 |
| (Gain) loss on derivative financial instruments | **$ 38.8** | $ (26.0) | **$ 6.8** | $ (8.9) | $ (9.8) |
| Asset impairments | **$ 70.0** | $ - | **$ 70.0** | $ 7.0 | $ 12.0 |
| Foreign exchange (gain) loss on long-term debt and investments, net | **$ 16.2** | $ 0.1 | **$ 28.3** | $ (9.5) | $ (20.3) |
| Prince George Pulp & Paper mill fire, net | **$ -** | $ - | **$ (8.5)** | $ - | $ - |
| North Central Plywoods mill fire, net | **$ -** | $ (57.9) | **$ (57.9)** | $ - | $ - |
| Interest expense, net | **$ 6.7** | $ 5.7 | **$ 17.7** | $ 2.4 | $ 5.1 |
| Amortization | **$ 42.2** | $ 41.5 | **$ 127.2** | $ 45.6 | $ 136.9 |
| **EBITDA, as reported** | **$ 55.1** | **$ 62.3** | **$ 43.3** | **$ (6.5)** | **$ (11.4)** |
| Restructuring, mill closure and severance costs | **$ 5.4** | $ 34.0 | **$ 43.2** | $ 11.1 | $ 19.8 |
| **EBITDA, as adjusted** | **$ 60.5** | **$ 96.3** | **$ 86.5** | **$ 4.6** | **$ 8.4** |
| Log inventory reversal resulting from new inventory accounting standard, included in EBITDA | **$ 3.9** | $ 72.4 | **$ 34.3** | $ - | $ - |

The troubled U.S. housing market continued to weigh heavily on the financial performance of the Company's lumber and panel businesses in the third quarter of 2008. U.S. housing starts continued their downward trend through the quarter, and inventory levels of new and existing homes, while showing a very modest decline, remained at historically high levels. Conditions deteriorated further in September, amid the unfolding U.S. and global financial and credit market crisis and heightened fears of a prolonged U.S. economic downturn.

The Company continued to adjust its production to lower market demand in the third quarter. In addition to its already indefinitely idled Mackenzie and Chetwynd lumber and PolarBoard OSB operations, the Company took production downtime at all of its solid wood operations in the third quarter, in the form of two week summer vacation shutdowns. In early October, the Company announced the indefinite closure of its Tackama plywood plant in Fort Nelson, B.C., due to weak plywood demand and prices.

Sales activity for solid wood products was lacklustre in the quarter, but with product in tight supply, prices edged up steadily in July and August. However, the turmoil in financial markets coupled with further weakness in the U.S. economy led to prices spiralling downwards in September, eliminating earlier gains.

Pulp market conditions softened during the third quarter in the face of weakening global demand and rising world inventories, and as a result prices came under significant pressure towards the end of the quarter.

On a more positive note, the Canadian dollar fell versus the US dollar in the quarter, declining three cents relative to the previous quarter, and ending the quarter at US$0.943.

EBITDA for the third quarter of 2008 was $55.1 million, down $7.2 million compared to the second quarter of 2008, but up $61.6 million compared to the third quarter of 2007. Adjusted EBITDA for the third quarter of 2008 was down $35.8 million compared to the previous quarter, but up $55.9 million compared to the third quarter of 2007. The second quarter's earnings included $72.4 million of income arising from the combination of a seasonal drawdown of logs previously written down to net realizable value, and the reversal of previously recorded log inventory write-downs. Log inventory adjustments at the end of the third quarter did not materially impact operating earnings, as volume levels were similar at the respective quarter ends, and the impact of weaker finished product prices on log write-downs was tempered by the weaker Canadian dollar and lower log costs.

Excluding the impact of log inventory reversals, the improved third quarter's EBITDA and Adjusted EBITDA reflected higher average lumber and OSB prices, the weaker Canadian dollar, further cost reductions at the Company's B.C. Interior operations, and the absence of Canfor Pulp Limited Partnership's (CPLP) second quarter scheduled maintenance outages.

Total shipment volumes of solid wood products were down 23% compared to the previous quarter, and 32% versus the third quarter of 2007, due substantially to reduced production levels in response to weaker demand. Compared to the previous quarter, average Western Spruce/Pine/Fir (SPF) lumber 2x4 #2 and Better prices increased US$33 per thousand board feet (Mfbm) to US$263 per Mfbm, but prices for Southern Yellow Pine (SYP) 2x4 #2 and Better lumber decreased US$5 per Mfbm to US$289 per Mfbm. Over the same period, OSB 7/16" North Central prices increased US$28 per thousand square feet (Msf) to US$202 per Msf, while plywood prices fell $4 per Msf to $333 per Msf. Average NBSK pulp list prices for U.S. delivery remained at an average of US$880 per tonne, but weakening fundamentals resulted in price erosion late in the quarter. Other pulp and specialty paper sales realizations showed a modest improvement in the quarter. The steep decline of SPF and SYP lumber prices in September resulted in higher finished lumber inventory write-downs at the end of the quarter, in contrast to the second quarter when lower write-downs of finished product inventories were recorded as a result of improving prices and lower inventoried costs at the end of June.

The Company recorded restructuring, severance and closure costs of $5.4 million in the third quarter of 2008, which related principally to indefinitely closed operations.

Other significant items affecting comparability with prior periods include the following:

- An asset impairment charge of $70.0 million ($56.9 million, after tax) related to investments in Howe Sound Pulp and Paper Limited Partnership (HSLP). The Company's investments include a 50% interest in Coastal Fibre Limited Partnership (CFLP), an entity which supplies fibre and related services to HSLP. The impairment reflects the continuing deterioration of B.C. Coastal pulp, paper and fibre market conditions;
- A foreign exchange translation loss on the Company's US-dollar denominated debt, net of investments, of $16.2 million as a result of the weaker Canadian dollar; and
- Losses of $38.8 million recorded on the Company's derivative financial instruments, principally as a result of a sharp decrease in energy prices, but also on foreign exchange derivatives. See additional commentary in "Non-Segmented Items" section.

## OPERATING RESULTS BY BUSINESS SEGMENT

### Lumber

**Selected Financial Information and Statistics**

| (millions of dollars unless otherwise noted) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| Sales | **$ 378.8** | $ 395.3 | **$ 1,126.6** | $ 507.2 | $ 1,547.4 |
| EBITDA [6] | **$ 15.3** | $ 46.3 | **$ (31.4)** | $ (50.5) | $ (124.5) |
| Adjusted EBITDA [6] | **$ 18.4** | $ 57.4 | **$ (16.5)** | $ (40.0) | $ (109.9) |
| EBITDA margin [6] | **4%** | 12% | **-3%** | -10% | -8% |
| Adjusted EBITDA margin [6] | **5%** | 15% | **-1%** | -8% | -7% |
| Operating income (loss) [6] | **$ (8.2)** | $ 22.8 | **$ (104.2)** | $ (75.9) | $ (201.7) |
| Average SPF 2x4 #2 & Better lumber price in US$ [7] | **$ 263** | $ 230 | **$ 233** | $ 260 | $ 257 |
| Average SPF price in Cdn$ | **$ 274** | $ 232 | **$ 237** | $ 271 | $ 284 |
| Average SYP 2x4 #2 lumber price in US$ [8] | **$ 289** | $ 294 | **$ 289** | $ 273 | $ 281 |
| Average SYP price in Cdn$ | **$ 301** | $ 296 | **$ 295** | $ 285 | $ 311 |
| Production – SPF lumber (MMfbm) | **747.1** | 877.0 | **2,507.8** | 1,050.3 | 3,244.8 |
| Production – SYP lumber (MMfbm) | **99.6** | 104.4 | **310.0** | 96.1 | 295.9 |
| Shipments - Canfor-produced SPF lumber (MMfbm)[9] | **755.9** | 935.3 | **2,553.9** | 1,121.1 | 3,245.1 |
| Shipments - Canfor-produced SYP lumber (MMfbm)[9] | **110.3** | 125.9 | **346.5** | 111.2 | 345.4 |
| Shipments - wholesale lumber (MMfbm) | **39.8** | 46.0 | **135.3** | 69.0 | 268.0 |

[6] EBITDA, Adjusted EBITDA and Operating income (loss) for the third quarter of 2008 included income of $0.9 million relating substantially to the reversal of previously recognized log inventory write-downs (lower log costs and the weaker Canadian dollar combined to offset the impact of weaker finished product prices). EBITDA for the second quarter of 2008 included income of $56.0 million largely due to the seasonal drawdown of logs previously written down to net realizable value, and the reversal of previously recognized log inventory write-downs.
[7] Western Spruce/Pine/Fir, per thousand board feet (Source – Random Lengths Publications, Inc.)
[8] Southern Yellow Pine, Eastside, per thousand board feet (Source – Random Lengths Publications, Inc.)
[9] Includes shipments of lumber purchased for remanufacture.

Overview

The Lumber segment reported an operating loss of $8.2 million for the third quarter of 2008, down $31.0 million compared to the second quarter of 2008, but an improvement of $67.7 million compared to the third quarter of 2007. Over those same periods, Adjusted EBITDA was down $39.0 million and up $58.4 million, respectively. Sales and production volumes were down significantly relative to the second quarter and the third quarter last year, reflecting weaker market demand.

The decrease in EBITDA and Adjusted EBITDA relative to the second quarter included the significant reversal of log inventory write-downs in the previous quarter. After taking this into account, Adjusted EBITDA was up $16 million, principally as a result of higher average SPF prices, the weaker Canadian dollar and lower log and natural gas costs. These positive factors more than offset the effect of deteriorating SPF and SYP prices on quarter end lumber inventory values (in contrast to the previous quarter end when there was a reversal of previously recognized write-downs that resulted from improved prices and lower inventoried costs).

Compared to the third quarter of 2007, the increase in Adjusted EBITDA reflected lower manufacturing costs achieved in the face of significant production downtime in the current period. Modest increases in SYP lumber and residual chip prices, as well as lower finished product inventory write-downs in the current period, also contributed to the improved results.

Markets

Demand for lumber in the U.S. continued to decline in the third quarter of 2008. U.S. housing starts were down 146,000 units SAAR, or 14%[10], compared to the previous quarter, and down 418,000 units SAAR, or 32%, compared to the third quarter of 2007. Single family starts continued to fall during the quarter, decreasing 11%[10] compared to the previous quarter and 39% compared to the same quarter of 2007.

Inventories of new homes for sale continued to decline slowly in the third quarter, and were down 38,000[10] units, or 8%, compared to the previous quarter, and down 128,000 units, or 23%, compared to the third quarter of 2007. As a result of slow home sales activity, however, the inventory of existing homes for sale remained largely unchanged from the previous quarter at 10.6 months[11], but was higher than the third quarter of 2007 level of 9.8 months[11].

Canadian housing starts, while still high by historical standards, declined to an average of 210,000 units SAAR in the third quarter of 2008, down 11,000 units SAAR[12] compared to the previous quarter, and down 34,000 units SAAR, or 14%, compared to the third quarter of 2007. Offshore demand remained relatively strong as Japanese 2x4 housing starts increased through the quarter.

Sales

Lumber sales for the third quarter of 2008 were down $16.5 million, or 4%, compared to the second quarter of 2008, and down $128.4 million, or 25%, compared to the third quarter of 2007.

The average price for SPF 2X4 #2 & Better was up US$33 per Mfbm, or 14%, compared to the previous quarter, and up slightly (US$3 per Mfbm, or 1%) compared to the third quarter of 2007. Average prices for SYP lumber, measured by 2x4 #2 & Better, were down US$5 per Mfbm, or 2%, compared to the previous quarter, and up US$16 per Mfbm, or 6%, versus the comparative quarter last year. Canadian dollar sales realizations were positively impacted by a 3% increase in the value of the U.S. dollar relative to the previous quarter, but compared to the same quarter a year ago, the CDN$/US$ exchange rate was substantially unchanged.

The Random Lengths Framing Lumber Composite price averaged US$273 per Mfbm for the third quarter of 2008 (up US$8 per Mfbm compared to the previous quarter), well below the trigger price of US$315 per Mfbm required to reduce the export tax rate on all U.S. bound shipments below the current rate of 15%.

Shipments for the third quarter of 2008 were down 201 million board feet, or 18%, compared to the previous quarter. The decline primarily reflected continued weakness in demand. Shipments were down 395 million board feet, or 30%, compared to the third quarter of 2007, reflecting significant market-related curtailment taken in the current period.

Residual chip sales revenues were well down relative to both comparable periods, due to the significantly lower sawmill operating rates. Average chip prices were in line with those for the previous quarter, and higher compared to the same quarter of 2007.

[10] U.S. Bureau of the Census
[11] National Association of Realtors
[12] CMHC

Operations

Lumber production for the third quarter was 847 million board feet, 135 million board feet, or 14%, lower than for the previous quarter and 300 million board feet, or 26%, lower than for the same quarter in 2007. Production for the current period reflected summer shuts, the indefinite closures of the Mackenzie (June) and Chetwynd (March) sawmills, and relative to the same quarter of 2007, a reduced number of shifts. Production in 2008 includes the Darlington sawmill in South Carolina, which was acquired in late 2007.

Despite significantly lower operating rates, conversion costs in the third quarter showed only a slight increase compared to the previous quarter and the same quarter of 2007, as the Company achieved another solid operating performance in the period. Compared to the previous quarter, log costs continued to trend lower in the period, primarily due to reductions to B.C. Interior stumpage rates and lower operating and overhead costs. The reduction in stumpage costs mostly reflected the Company's consumption of a higher mix of lower grade logs (infected by the mountain pine beetle). The same factors, combined with lower market stumpage rates, accounted for the significant majority of the favourable variance compared to the same quarter of 2007.

As a result of the above factors, the Company's unit cash manufacturing costs at its Western Canadian operations were down 4% compared to the second quarter of 2008 and down 13% compared to the third quarter of 2007, despite additional curtailment of approximately 130 million and 330 million board feet compared to those respective periods.

## Panels

**Selected Financial Information and Statistics**

| (millions of dollars unless otherwise noted) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| Sales | **$ 36.0** | $ 59.9 | **$ 149.8** | $ 73.9 | $ 227.2 |
| EBITDA[13] | **$ (0.1)** | $ (7.3) | **$ (29.8)** | $ (2.0) | $ (24.7) |
| Adjusted EBITDA [13] | **$ 2.2** | $ 15.4 | **$ (2.0)** | $ (2.0) | $ (24.6) |
| EBITDA margin[13] | **0%** | -12% | **-20%** | -3% | -11% |
| Adjusted EBITDA margin [13] | **6%** | 26% | **-1%** | -3% | -11% |
| Operating loss [13] | **$ (3.4)** | $ (11.5) | **$ (41.7)** | $ (7.5) | $ (42.3) |
| Average plywood price in Cdn$[14] | **$ 333** | $ 337 | **$ 339** | $ 394 | $ 377 |
| Average OSB price in US$[15] | **$ 202** | $ 174 | **$ 171** | $ 177 | $ 159 |
| Average OSB price in Cdn$ | **$ 210** | $ 176 | **$ 174** | $ 185 | $ 176 |
| Production – plywood (MMsf 3/8") | **44.1** | 85.7 | **219.6** | 89.8 | 291.9 |
| Production – OSB (MMsf 3/8") | **85.3** | 134.3 | **378.0** | 158.8 | 505.6 |
| Shipments – plywood (MMsf 3/8") | **54.2** | 95.7 | **235.9** | 89.5 | 295.1 |
| Shipments – OSB (MMsf 3/8") | **90.5** | 152.9 | **407.2** | 161.8 | 503.6 |

[13] EBITDA, Adjusted EBITDA and Operating income (loss) for the third quarter of 2008 included a log inventory recovery of $3.0 million relating substantially to lower inventory volumes on which write-downs were applied. EBITDA for the second quarter of 2008 included a recovery of $16.4 million relating to the seasonal drawdown of logs, which had been previously written down to net realizable value, and the reversal of previously recognized log inventory write-downs.
[14] Canadian softwood plywood, per Msf 3/8" basis, delivered to Toronto (Source – C.C. Crowe Publications, Inc.)
[15] OSB, per Msf 7/16" North Central (Source – Random Lengths Publications, Inc.)

Overview

The Panels segment recorded an operating loss of $3.4 million for the third quarter, an improvement of $8.1 million from the previous quarter, and $4.1 million compared to the third quarter of 2007. The operating loss in the second quarter included significant restructuring, mill closure and severance costs related to the Company's North Central Plywoods (NCP) and PolarBoard operations.

Adjusted EBITDA was down $13.2 million compared to the previous quarter, but up $4.2 million compared to the third quarter of 2007. The decrease in Adjusted EBITDA compared to the previous quarter was principally due to a significant reversal of previous log inventory write-downs in the second quarter. Results in the third quarter also reflected higher OSB sales realizations but these gains were offset by higher wax and resin costs and weaker plywood realizations.

Compared to the same quarter of 2007, the current period's log inventory recovery, higher OSB prices and lower log costs more than offset significantly lower plywood prices and increased wax and resin costs.

Markets

Panel markets continued to be mixed in the third quarter of 2008. OSB prices moved up through July and August primarily as a result of industry curtailments but prices fell sharply in September in the wake of financial market and economic developments. Plywood prices remained weak through the quarter.

Sales

OSB prices averaged US$202 per thousand square feet for the third quarter of 2008, up US$28, or 16%, from the previous quarter and 14% from the third quarter of 2007. The Canadian softwood plywood 3/8" delivered Toronto price was down $4, or 1%, from the previous quarter, and down $61, or 15%, from the third quarter of 2007. Total shipment volumes were down 42% compared to both the previous quarter and the third quarter of 2007, principally as a result of the fire that destroyed the NCP facility in Prince George, B.C. in late May, and the indefinite closure of the PolarBoard mill in June.

Operations

Production in the third quarter reflected the lower operating rates, with volumes down 41% and 48% versus the previous quarter and third quarter of 2007, respectively. Unit cash manufacturing costs were in line with those for the previous quarter, with lower log costs and productivity improvements offsetting higher OSB wax and resin costs.

### Pulp and Paper[16]

**Selected Financial Information and Statistics**

| (millions of dollars unless otherwise noted) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| Sales | **$ 253.2** | $ 251.2 | **$ 746.5** | $ 256.3 | $ 790.0 |
| EBITDA | **$ 45.1** | $ 26.6 | **$ 116.7** | $ 49.7 | $ 162.8 |
| EBITDA margin | **18%** | 11% | **16%** | 19% | 21% |
| Operating income | **$ 31.5** | $ 14.3 | **$ 79.0** | $ 36.1 | $ 124.3 |
| Average pulp price delivered to U.S. – US$[17] | **$ 880** | $ 880 | **$ 880** | $ 837 | $ 812 |
| Average price in Cdn$ | **$ 917** | $ 889 | **$ 896** | $ 875 | $ 897 |
| Production – pulp (000 mt) | **307.8** | 276.2 | **868.5** | 317.1 | 931.3 |
| Production – paper (000 mt) | **35.9** | 34.2 | **102.5** | 33.0 | 98.5 |
| Shipments – Canfor-produced pulp (000 mt) | **284.0** | 289.4 | **852.4** | 307.0 | 920.6 |
| Pulp marketed on behalf of HSLP (000 mt)[18] | **86.0** | 96.2 | **260.5** | 89.4 | 273.3 |
| Shipments – paper (000 mt) | **31.7** | 33.7 | **100.5** | 30.8 | 97.1 |

[16] Includes the Taylor Pulp Mill and 100% of Canfor Pulp Limited Partnership (CPLP), which is consolidated in Canfor's operating results. Pulp production and shipment volumes presented are for both northern bleached softwood kraft (NBSK) and bleached chemi-thermo mechanical pulp (BCTMP).
[17] Per tonne, NBSK pulp list price delivered to U.S. (RISI)
[18] Howe Sound Pulp and Paper Limited Partnership Pulp Mill

Overview

Operating income and EBITDA in the Pulp and Paper segment in the third quarter of 2008 were up $17.2 million and $18.5 million, respectively, from the previous quarter. The favourable variances resulted primarily from the absence of scheduled maintenance outages in the third quarter, and the positive impact on sales realizations from the weaker Canadian dollar, partly offset by higher freight costs on inputs and shipments of finished product.

Compared to the same quarter of 2007, operating income and EBITDA were both down $4.6 million. The decrease was mostly attributable to higher fibre, chemical, energy and freight costs, and a lower-value region sales mix, all of which more than offset the favourable impact of higher quarter-over-quarter prices.

Markets

Pulp market conditions weakened during the third quarter of 2008. Market pulp inventories (World 20 Producers) of softwood kraft market pulp were at 36 days of supply[19] at the end of the third quarter, an increase of 7 days from the level at the end of the second quarter. Inventories of 30 days are generally considered to be representative of a balanced market. Shipments of NBSK market pulp were lower by 2.9% compared to the same period in 2007.

Weakening paper demand in the third quarter resulted in a reduction of wood pulp purchases by papermakers, causing pulp inventories held by producers to rise, and pulp prices to fall in all major markets. Northern European NBSK prices finished the third quarter at US$850 per tonne (a decrease of US$50 per tonne from the beginning of the quarter). While the average NBSK pulp list price delivered to the U.S. was unchanged from the previous quarter, at US$880 per tonne, average transaction prices fell $15 per tonne during the quarter (from US$885 per tonne in July to US$870 per tonne in September).

Sales

Shipments of Canfor-produced pulp were down 2% compared to the previous quarter. Realized pulp and paper prices in Canadian dollars in the third quarter showed a modest increase over the previous quarter, reflecting the positive impact of the weaker Canadian dollar which outweighed higher freight costs. Realized pulp and paper prices were also up compared to the third quarter of 2007, but this was mostly offset by significantly higher freight costs and a lower-value sales mix.

Operations

Overall unit manufacturing costs for the third quarter of 2008 were down compared to the previous quarter due principally to scheduled maintenance outages in the second quarter, and lower operating, labour and maintenance costs, which outweighed the impact of higher delivered fibre and chemical costs. Unit manufacturing costs were up compared to the same quarter of 2007, primarily due to increased fibre costs (reflecting a combination of additional whole log chipping and higher freight costs) and higher chemical and energy costs in the current period.

[19] Pulp and Paper Products Council (PPPC)

**Non-Segmented Items**

| (millions of dollars unless otherwise noted) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| Corporate costs | **$ (7.1)** | $ (4.9) | **$ (17.0)** | $ (4.8) | $ (28.6) |
| Interest expense, net | **$ (6.7)** | $ (5.7) | **$ (17.7)** | $ (2.4) | $ (5.1) |
| Foreign exchange gain (loss) on long-term debt and investments, net | **$ (16.2)** | $ (0.1) | **$ (28.3)** | $ 9.5 | $ 20.3 |
| Gain (loss) on derivative instruments | **$ (38.8)** | $ 26.0 | **$ (6.8)** | $ 8.9 | $ 9.8 |
| Asset impairments | **$ (70.0)** | $ - | **$ (70.0)** | $ (7.0) | $ (12.0) |
| Prince George Pulp & Paper mill fire, net | **$ -** | $ - | **$ 8.5** | $ - | $ - |
| North Central Plywoods mill fire, net | **$ -** | $ 57.9 | **$ 57.9** | $ - | $ - |
| Other income (expense), net | **$ 0.1** | $ (1.5) | **$ (0.2)** | $ (9.3) | $ (7.8) |

Corporate costs for the three months ended September 30, 2008 were up $2.2 million compared to the second quarter of 2008, and were $2.3 million higher than for the third quarter of 2007, primarily as a result of long-term incentive costs recorded in the current period. For the nine months ended September 30, 2008, corporate costs were $11.6 million lower than for the same period in 2007, due mainly to reduced staffing and other cost reduction initiatives, and costs associated with the resignation of the Company's former chief executive officer recorded in 2007.

Net interest expense for the third quarter was $6.7 million, taking the total for the nine months of 2008 to $17.7 million. This represents an increase of $12.6 million compared to the first nine months of 2007, and reflected higher net indebtedness in 2008.

In the third quarter of 2008, the Company recorded a foreign exchange translation loss on its US-dollar denominated debt, net of investments, of $16.2 million, as a result of a weaker Canadian dollar.

The Company uses a variety of derivative financial instruments as partial economic hedges against unfavourable changes in natural gas and diesel costs, foreign exchange rates and lumber prices. In the third quarter of 2008, the Company recorded a loss of $38.8 million related to its derivative instruments. For the most part, this reflected a sharp decline in natural gas prices in the third quarter, but unrealized losses were also recorded on diesel and foreign exchange derivatives. The following table summarizes the amounts of the various components for the comparable periods.

Gain (Loss) on Derivative Financial Instruments:

| | 3 months ended September 30, | | 9 months ended September 30, | |
|---|---|---|---|---|
| (millions of dollars) | **2008** | 2007 | **2008** | 2007 |
| Natural gas swaps | **$ (25.3)** | $ (6.1) | **$ 5.8** | $ (10.2) |
| Diesel options and swaps | **(3.5)** | 0.2 | **8.0** | 4.9 |
| Foreign exchange collars | **(9.4)** | 15.2 | **(20.6)** | 15.1 |
| Lumber futures | **(0.6)** | (0.4) | **-** | - |
| | **$ (38.8)** | $ 8.9 | **$ (6.8)** | $ 9.8 |

In the third quarter of 2008, the Company recorded an asset impairment charge of $70.0 million ($56.9 million after tax) related to investments in HSLP. The Company's investments include a 50% interest in CFLP, which supplies fibre and related services to HSLP. The impairment reflects the continuing deterioration of B.C. Coastal pulp, paper and fibre market conditions.

## SUMMARY OF FINANCIAL POSITION

The following table summarizes Canfor's cash flow and financial position as at the end of the following periods:

| (millions of dollars) | Q3 2008 | Q2 2008 | YTD 2008 | Q3 2007 | YTD 2007 |
|---|---|---|---|---|---|
| Increase (decrease) in cash and cash equivalents | **$ 36.6** | $ 56.1 | **$ 38.7** | $ (60.2) | $ (620.0) |
| Operating activities | **$ 63.3** | $ 80.2 | **$ 136.8** | $ 102.7 | $ (432.2) |
| Financing activities | **$ (14.0)** | $ (11.9) | **$ (50.5)** | $ (56.2) | $ (148.5) |
| Investing activities | **$ (12.7)** | $ (12.2) | **$ (47.6)** | $ (106.7) | $ (39.3) |
| Ratio of current assets to current liabilities | | | **2.3 : 1** | | 3.1 : 1 |
| Ratio of net debt to capitalization | | | **10.0%** | | 5.0% |

### Changes in Financial Position

Operating activities generated $63.3 million of cash in the third quarter of 2008, compared to $80.2 million in the previous quarter, and $102.7 million in the third quarter of 2007. The decrease relative to the previous quarter primarily reflected the seasonal drawdown of log inventories in the B.C. Interior through the spring break-up period, and the Company's replacement of its diesel forward contracts with options (net proceeds - $11.0 million), partly offset by improved cash operating earnings. Cash flow from operations in the third quarter of 2007 reflected a favourable movement in working capital, including a significant drawdown of inventories. The significant decrease in cash and cash equivalents for the nine months ended September 30, 2007 resulted primarily from the payment of taxes related to a countervailing and anti-dumping duty refund received by Canfor in late 2006, debt repayments and operating losses.

Financing activities used $14.0 million of cash in the third quarter of 2008, for the most part reflecting $12.8 million of CPLP distributions paid to non-controlling interests.

Investing activities, net totaled $12.7 million in the third quarter of 2008, and consisted principally of capital expenditures of $22.2 million less an initial advance of $10.0 million from the Company's insurers related to the NCP fire. Capital expenditures for the nine months ended September 30, 2008 were $58.3 million.

### Liquidity and Financial Requirements

In July 2008, Canfor Corporation increased its operating line of credit by $30.0 million. At September 30, 2008, the Company, on a consolidated basis, had cash and cash equivalents of $334.2 million and $439.0 million of bank operating lines of credit available, of which $4.1 million was drawn down and a further $44.5 million was reserved for several standby letters of credit. The Company's net debt to capitalization ratio at quarter end was 10.0%.

At September 30, 2008, the Company had in place foreign exchange collar contracts for US$501 million covering the period to December 2009. These contracts fix the company's exchange rate between a minimum of CDN$0.98 to US$1.00 and a maximum of CDN$1.13 to US$1.00.

### Asset-Backed Commercial Paper

The Company has US$81.2 million of non-bank asset-backed commercial paper (ABCP), which is invested in four different Canadian trusts (the Trusts) with original maturities between August and September of 2007. Since August of 2007, the market for ABCP has experienced significant liquidity problems. The Trusts failed to make payment at maturity and, along with 16 other ABCP conduits, are subject to restructuring under the Pan Canadian Investors Committee for the Third Party Asset Backed Commercial Paper (the Pan Canadian Investors Committee).

On March 17, 2008, the Pan Canadian Investors Committee filed with the Ontario Superior Court of Justice (the Court) a comprehensive arrangement pursuant to the Companies Creditors Arrangement Act (CCAA) to restructure most similarly affected trusts. On April 25, noteholders voted overwhelmingly in favour of the restructuring plan. On June 5, 2008, the Court approved the Pan Canadian Investors Committee plan to restructure the 20 ABCP conduits. Following an unsuccessful appeal by certain investors to the Ontario Court of Appeal, the Supreme Court of Canada on September 19 denied the plaintiffs further leave to appeal. The restructuring plan is currently expected to be completed by the end of 2008.

With respect to estimating the fair value of the ABCP, quoted market values of the investments have not been available. Therefore, management's judgment has been applied using all currently available information and estimated assumptions that market participants would use in pricing such ABCP. In estimating fair value, Canfor has assumed a high likelihood of successful restructuring of the investment.

Based on its assessment of fair value, Canfor recognized an impairment loss of $16.2 million in 2007 related to these investments, which represented 20% of the face value. No adjustment was recorded in the third quarter of 2008. It is possible that further information will become available on the actual composition of the referenced assets. A change in the estimate of the composition of the referenced assets would affect the valuation. In addition, if sales of the restructured senior or subordinated notes occur in the future, these sales might represent observable market transactions that could appropriately be used to determine the fair value of the investment.

## AGREEMENT FOR SALE OF PANEL AND FIBRE PROPERTY

On April 11, 2008, the Company signed an agreement with the Vancouver Fraser Port Authority (VFPA) for the sale of a property ("Sale Agreement") located in New Westminster, British Columbia. The agreed sales consideration is $47.5 million, which will result in a pre-tax gain on disposal of substantially the same amount. The property was the site of the Company's former Panel and Fibre mill, which closed down in December 2007. Related closure costs of $14.4 million were recorded in the fourth quarter of 2007.

Following the signing of the Sale Agreement, the Greater Vancouver Sewage and Drainage District ("Metro Vancouver") filed an expropriation notice against title to the subject lands, which prevented the Company from transferring legal title to the purchaser on the closing of the Sale Agreement. The VFPA has commenced an action against Metro Vancouver to remove the expropriation notice. In the event that the land is expropriated, under the Expropriation Act, Metro Vancouver is required to pay the Company fair value for the property.

The timing and ultimate outcome of this transaction is not determinable at this time and no amounts related to this transaction have been recorded in the third quarter of 2008.

## OUTLOOK

### Lumber and Panel Markets

There remains no immediate end in sight to the extremely challenging North American structural lumber market conditions. Although U.S. home builders have significantly reduced home construction in an effort to reduce new and existing home inventories, their efforts have been hampered by the effects of an ailing U.S. economy, falling home prices, and the current upheaval in financial and credit markets. Any meaningful recovery in the U.S. housing market is now not expected before the end of 2009, with much depending on both the success of recent government responses to unprecedented credit and liquidity problems, and the severity and length of the U.S. economic downturn.

Lumber demand from the repair and remodeling sector in the U.S. is also expected to continue to decrease, due to falling home prices and the difficulties being experienced by home owners in obtaining financing. Housing starts in Canada are expected to continue to fall throughout the rest of the year, and remain low in 2009.

### Pulp and Paper Markets

Due to general weakness and the global financial crisis, there is a slowdown in pulp demand which is resulting in an increase in inventories and decreasing prices. The impact of price declines in terms of US dollars is mitigated by lower oil and natural gas prices and a weakened Canadian dollar. However, with rising inventories, CPLP has decided to take market related production curtailments of approximately 30,000 tonnes of pulp and 10,000 tonnes of kraft paper. These curtailments are expected to occur over the next several months.

## OUTSTANDING SHARES

At October 29, 2008, there were 142,589,312 common shares outstanding.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements. On an ongoing basis, management reviews its estimates, including those related to useful lives for amortization, impairment of long-lived assets, certain accounts receivable, pension and other employee future benefit plans and asset retirement obligations based upon currently available information. While it is reasonably possible that circumstances may arise which cause actual results to differ from these estimates, management does not believe it is likely that any such differences will materially affect the Company's financial condition.

## ACCOUNTING POLICY CHANGES

Effective January 1, 2008, the Company adopted the Canadian Institute of Chartered Accountants' new Handbook Sections: 1535 "Capital Disclosures", 3031 "Inventories", 3862 "Financial Instruments – Disclosures" and 3863 "Financial Instruments – Presentation". Handbook sections 3862 and 3863 replace section 3861 "Financial Instruments – Disclosure and Presentation". These recommendations have been incorporated into the unaudited interim consolidated financial statements.

*Section 1535 – Capital Disclosures*

This Section establishes standards for disclosing information about an entity's capital and how it is managed. Under this standard the Company is required to disclose qualitative and quantitative information that enables users of the financial statements to evaluate the Company's objectives, policies and processes for managing capital.

*Section 3031 - Inventories*

This Section replaced Section 3030 – "Inventories" and provides significantly more guidance on the measurement of inventories, with an expanded definition of cost, and the requirement that inventories must be measured at the lower of cost and net realizable value. In addition, the section sets out additional disclosure requirements, including accounting policies, carrying values, and the amount of any inventory write-downs. In conjunction with section 3061 "Property Plant and Equipment", it also provides guidance on the classification of major spare parts and stand-by equipment.

On January 1, 2008, the Company adopted the new recommendations on a prospective basis. As a result of implementing these standards, inventories decreased by $60.6 million (log inventories by $46.5 million, processing materials and supplies by $14.1 million), property, plant and equipment increased by $14.1 million, future income tax liabilities decreased by $15.9 million and opening retained earnings were reduced by $30.6 million.

Total log and finished product inventory write-downs as of September 30, 2008 were $22.2 million.

*Section 3862 – Financial Instruments – Disclosures*

This Section requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate: (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks.

*Section 3863 – Financial Instruments – Presentation*

This Section establishes standards for presentation of financial instruments and non-financial derivatives.

## FUTURE ACCOUNTING POLICY CHANGES

In February 2008, the CICA issued a new accounting standard, Handbook Section 3064, *Goodwill and Intangible Assets*. This section replaces CICA Handbook Section 3062, *Goodwill and Intangible Assets*, and establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of various preproduction and start-up costs and requires that these costs be expensed as incurred. This standard will be applicable to the Company for annual and interim accounting periods beginning on January 1, 2009. The Company does not expect that this standard will have a material impact on its consolidated financial statements.

## CONVERSION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

On February 13, 2008, the Accounting Standards Board announced that publicly accountable entities will be required to prepare financial statements in accordance with International Financial Reporting Standards ("IFRS") for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. The Company is currently in the process of developing a conversion implementation plan, has appointed a dedicated project manager and is assessing the impacts of the conversion on the consolidated financial statements and disclosures of the Company.

## INTERNAL CONTROLS OVER FINANCIAL REPORTING

During the quarter ending September 30, 2008, there were no changes in the Company's internal controls over financial reporting that materially affected, or would be reasonably likely to materially affect, such controls.

## RISKS AND UNCERTAINTIES

A comprehensive discussion of risks and uncertainties is included in the Company's 2007 annual statutory reports which are available on www.sedar.com or www.canfor.com.

## SELECTED QUARTERLY FINANCIAL INFORMATION

| | **Q3 2008** | Q2 2008 | Q1 2008 | Q4 2007 | Q3 2007 | Q2 2007 | Q1 2007 | Q4 2006 |
|---|---|---|---|---|---|---|---|---|
| **Sales and Income** (millions of dollars) | | | | | | | | |
| Sales | **$ 668.0** | $ 706.4 | $ 648.5 | $ 711.0 | $837.4 | $876.6 | $850.6 | $ 892.0 |
| Operating income (loss) | **$ 12.8** | $ 20.8 | $(117.5) | $(124.7) | $(52.1) | $(38.4) | $(57.8) | $ 656.1 |
| Net income (loss) from continuing operations | **$ (94.2)** | $ 64.2 | $ (85.4) | $(237.0) | $(42.1) | $(38.8) | $(42.7) | $ 466.9 |
| Net income (loss) | **$ (94.2)** | $ 64.2 | $ (85.4) | $(237.0) | $(42.1) | $(38.8) | $(42.7) | $ 465.3 |
| **Per common share** (dollars) | | | | | | | | |
| Net income (loss) from continuing operations | | | | | | | | |
| Basic | **$ (0.66)** | $ 0.45 | $ (0.60) | $ (1.66) | $ (0.30) | $ (0.27) | $ (0.30) | $ 3.28 |
| Diluted | **$ (0.66)** | $ 0.45 | $ (0.60) | $ (1.66) | $ (0.30) | $ (0.27) | $ (0.30) | $ 3.27 |
| **Net income (loss)** | | | | | | | | |
| Basic and diluted | **$ (0.66)** | $ 0.45 | $ (0.60) | $ (1.66) | $ (0.30) | $ (0.27) | $ (0.30) | $ 3.26 |
| **Statistics** | | | | | | | | |
| Lumber shipments (MMfbm) | **906** | 1,107 | 1,023 | 1,149 | 1,301 | 1,345 | 1,213 | 1,352 |
| Plywood shipments (MMsf 3/8”) | **54** | 96 | 86 | 90 | 90 | 119 | 87 | 110 |
| OSB shipments (MMsf 3/8”) | **91** | 153 | 164 | 166 | 162 | 168 | 174 | 184 |
| Pulp shipments (000 mt) | **284** | 289 | 279 | 308 | 307 | 309 | 304 | 292 |
| Average exchange rate (US$/Cdn$) | **$ 0.960** | $ 0.990 | $ 0.996 | $ 1.019 | $ 0.957 | $ 0.911 | $ 0.854 | $ 0.878 |
| Average Western SPF 2x4 #2&Btr lumber price (US $) | **$ 263** | $ 230 | $ 205 | $ 230 | $ 260 | $ 258 | $ 253 | $ 245 |
| Average SYP (East) 2x4 #2 lumber price (US $) | **$ 289** | $ 294 | $ 285 | $ 277 | $ 273 | $ 292 | $ 279 | $ 272 |
| Average plywood price – Toronto (Cdn $) | **$ 333** | $ 337 | $ 347 | $ 374 | $ 394 | $ 357 | $ 379 | $ 366 |
| Average OSB price – North Central (US $) | **$ 202** | $ 174 | $ 138 | $ 165 | $ 177 | $ 156 | $ 145 | $ 166 |
| Average NBSK pulp list price delivered to the U.S. (US $) | **$ 880** | $ 880 | $ 880 | $ 857 | $ 837 | $ 810 | $ 790 | $ 770 |

In addition to exposure to changes in product prices and foreign exchange, the Company’s financial results are impacted by seasonal factors such as weather and building activity. Adverse weather conditions can cause logging curtailments, which can affect the supply of raw materials to sawmills, plywood and OSB plants, and pulp mills. Market demand also varies seasonally to some degree. For example, building activity and repair and renovation work, which affects demand for lumber and panel products, is generally stronger in the spring and summer months. Shipment volumes are affected by these factors as well as by global supply and demand conditions, which as indicated in the lumber operations commentary, have adversely impacted the Company’s production since late 2006, and particularly in the three most recent quarters.

Following the spinout of the Pulp Business on July 1, 2006, Canfor continues to consolidate 100% of the income from CPLP (Canfor Pulp Limited Partnership). However, the 20% non-controlling interest is removed from the income statement beginning in the third quarter of 2006, and a further 29.8% at the end of November 2006, which affects comparability of net income of prior periods.

Other factors that impact the comparability of the quarters are noted below:

| (millions of dollars, after tax and non-controlling interests) | Q3 2008 | Q2 2008 | Q1 2008 | Q4 2007 | Q3 2007 | Q2 2007 | Q1 2007 | Q4 2006 |
|---|---|---|---|---|---|---|---|---|
| Gain (loss) on derivative financial instruments | **$(21.4)** | $ 14.5 | $ 2.7 | $ 3.5 | $ 6.9 | $ (3.7) | $ 4.9 | $ - |
| New inventory accounting standard | **2.5** | 47.8 | (29.0) | - | - | - | - | - |
| Foreign exchange gain (loss) on long-term debt and investments, net | **(11.3)** | - | (8.7) | (3.5) | 5.1 | 10.2 | (5.3) | (9.9) |
| Prince George Pulp & Paper mill fire, net | **-** | - | 3.6 | - | - | - | - | - |
| North Central Plywoods mill fire, net | **-** | 45.0 | - | - | - | - | - | - |
| Restructuring, mill closure and severance costs | **(3.6)** | (22.3) | (2.6) | (14.2) | (7.3) | (5.8) | - | (4.3) |
| Corporate income tax rate reductions | **-** | - | 9.1 | 35.8 | 0.9 | 1.0 | - | - |
| Duty refund and interest | **-** | - | - | - | 2.0 | - | 1.4 | 551.2 |
| CEO remuneration on resignation | **-** | - | - | - | - | - | (3.0) | - |
| Adjustment to incentive costs | **-** | - | - | 1.5 | - | 2.3 | - | - |
| Dividend income | **-** | - | - | - | - | - | 4.1 | - |
| Accrual for environmental and related liabilities | **-** | - | - | (1.9) | - | - | - | - |
| Prior year tax reassessments and other tax adjustments | **-** | - | - | 0.5 | 2.2 | - | - | 0.5 |
| Net income (loss) from discontinued operations | **-** | - | - | - | - | - | - | (1.6) |
| Asset impairments | **(56.9)** | - | - | (189.1) | (6.0) | - | (4.1) | (16.2) |
| Net favourable (unfavourable) impact on net income | **$(90.7)** | **$ 85.0** | **$(24.9)** | **$(167.4)** | **$ 3.8** | **$ 4.0** | **$ (2.0)** | **$519.7** |

## Canfor Corporation
## Consolidated Income Statements

| (millions of dollars, unaudited) | 3 months ended September 30, 2008 | 2007 | 9 months ended September 30, 2008 | 2007 |
|---|---|---|---|---|
| **Sales** | **$ 668.0** | $ 837.4 | **$ 2,022.9** | $ 2,564.6 |
| **Costs and expenses** | | | | |
| Manufacturing and product costs | **459.2** | 649.0 | **1,480.6** | 1,973.1 |
| Freight and other distribution costs | **114.3** | 141.5 | **359.1** | 437.5 |
| Export taxes | **17.5** | 26.5 | **49.1** | 84.4 |
| Amortization | **42.2** | 45.6 | **127.2** | 136.9 |
| Selling and administration costs | **16.6** | 15.8 | **47.6** | 61.2 |
| Restructuring, mill closure and severance costs (Note 2) | **5.4** | 11.1 | **43.2** | 19.8 |
| | **655.2** | 889.5 | **2,106.8** | 2,712.9 |
| **Operating income (loss)** | **12.8** | (52.1) | **(83.9)** | (148.3) |
| Interest expense, net | **(6.7)** | (2.4) | **(17.7)** | (5.1) |
| Foreign exchange gain (loss) on translation of long-term debt and investments, net | **(16.2)** | 9.5 | **(28.3)** | 20.3 |
| Gain (loss) on derivative financial instruments (Note 12) | **(38.8)** | 8.9 | **(6.8)** | 9.8 |
| North Central Plywoods mill fire, net (Note 4 (a)) | **-** | - | **57.9** | - |
| Prince George Pulp & Paper mill fire, net (Note 4 (b)) | **-** | - | **8.5** | - |
| Asset impairments (Note 8 (b)) | **(70.0)** | (7.0) | **(70.0)** | (12.0) |
| Other income (expense), net | **0.1** | (9.3) | **(0.2)** | (7.8) |
| Net loss before income taxes | **(118.8)** | (52.4) | **(140.5)** | (143.1) |
| Income tax recovery (Note 5) | **30.0** | 27.2 | **61.7** | 78.8 |
| Non-controlling interests | **(5.4)** | (16.9) | **(36.6)** | (59.3) |
| **Net loss** | **$ (94.2)** | $ (42.1) | **$ (115.4)** | $ (123.6) |
| **Per common share** (in dollars) (Note 6) | | | | |
| Net loss - Basic and Diluted | **$ (0.66)** | **$** (0.30) | **$ (0.81)** | $ (0.87) |

The accompanying notes are an integral part of these interim financial statements.

## Canfor Corporation
## Consolidated Cash Flow Statements

| (millions of dollars, unaudited) | 3 months ended September 2008 | 3 months ended September 2007 | 9 months ended September 2008 | 9 months ended September 2007 |
|---|---|---|---|---|
| **Cash generated from (used in)** | | | | |
| **Operating activities** | | | | |
| Net loss | **$ (94.2)** | $ (42.1) | **$ (115.4)** | $ (123.6) |
| Items not affecting cash: | | | | |
| Amortization | **42.2** | 45.6 | **127.2** | 136.9 |
| Income taxes | **(16.8)** | 1.3 | **(4.4)** | (2.8) |
| Long-term portion of deferred reforestation | **(10.2)** | (8.2) | **(9.7)** | (2.4) |
| North Central Plywoods mill fire, net (Note 4 (a)) | **-** | - | **(57.9)** | - |
| Prince George Pulp & Paper mill fire, net (Note 4 (b)) | **-** | - | **(8.5)** | - |
| Foreign exchange (gain) loss on translation of long-term debt | **20.5** | (34.1) | **35.0** | (88.4) |
| (Gain) loss on derivative financial instruments (Note 12) | **38.8** | (8.9) | **6.8** | (9.8) |
| Asset impairments (Note 8 (b)) | **70.0** | 7.0 | **70.0** | 12.0 |
| Non-controlling interests | **5.4** | 16.9 | **36.6** | 59.3 |
| Other | **9.2** | 9.9 | **14.7** | 19.7 |
| Net proceeds from replacement of derivative financial instruments | **-** | - | **11.0** | - |
| Salary pension plan contributions | **(4.1)** | (5.9) | **(8.7)** | (12.0) |
| Deferred scheduled maintenance spending | **(0.2)** | (0.2) | **(5.8)** | (2.3) |
| Net change in non-cash working capital (Note 7) | **2.7** | 121.4 | **45.9** | (418.8) |
| | **63.3** | 102.7 | **136.8** | (432.2) |
| **Financing activities** | | | | |
| Proceeds from long-term debt | **-** | 0.3 | **-** | 0.3 |
| Repayment of long-term debt | **-** | (37.8) | **(14.8)** | (91.1) |
| Changes in operating bank loans | **(1.2)** | 0.8 | **4.1** | 0.7 |
| Cash distributions paid to non-controlling interests | **(12.8)** | (19.6) | **(39.5)** | (58.6) |
| Other | **-** | 0.1 | **(0.3)** | 0.2 |
| | **(14.0)** | (56.2) | **(50.5)** | (148.5) |
| **Investing activities** | | | | |
| Change in temporary investments | **-** | 9.1 | **-** | 124.5 |
| Change in asset-backed commercial paper | **-** | (85.9) | **-** | (85.9) |
| Additions to property, plant, equipment and timber | **(22.2)** | (23.7) | **(58.3)** | (63.1) |
| Proceeds from disposal of property, plant and equipment | **0.1** | 2.2 | **4.3** | 2.8 |
| Proceeds from North Central Plywoods fire claim (Note 4 (a)) | **10.0** | - | **10.0** | - |
| Proceeds from Prince George Pulp & Paper mill fire damage claim | **-** | - | **8.0** | - |
| Advances to affiliated companies | **-** | - | **(11.5)** | - |
| Other | **(0.6)** | (8.4) | **(0.1)** | (17.6) |
| | **(12.7)** | (106.7) | **(47.6)** | (39.3) |
| **Increase (decrease) in cash and cash equivalents** | **36.6** | (60.2) | **38.7** | (620.0) |
| **Cash and cash equivalents at beginning of period** | **297.6** | 464.0 | **295.5** | 1,023.8 |
| **Cash and cash equivalents at end of period** | **$ 334.2** | $ 403.8 | **$ 334.2** | $ 403.8 |

| | | | | |
|---|---|---|---|---|
| **Cash payments (receipts) in the period** | | | | |
| Interest, net | **$ 6.1** | $ 4.3 | **$ 18.7** | $ 11.2 |
| Income taxes | **$ (12.1)** | $ (11.6) | **$ (135.7)** | $ 231.4 |

## Canfor Corporation
## Consolidated Balance Sheets

| (millions of dollars) | | **As at September 30, 2008** | | As at December 31, 2007 |
|---|---|---|---|---|
| **ASSETS** | | (unaudited) | | (audited) |
| **Current Assets** | | | | |
| Cash and cash equivalents | **$** | **334.2** | $ | 295.5 |
| Accounts receivable | | | | |
| Trade | | **202.6** | | 199.5 |
| Other (Note 4) | | **89.4** | | 74.3 |
| Income taxes recoverable | | **29.0** | | 136.7 |
| Inventories (Note 1(b)) | | **420.9** | | 472.0 |
| Prepaid expenses | | **49.9** | | 40.8 |
| Total current assets | | **1,126.0** | | 1,218.8 |
| **Long-term investments and other** (Note 8) | | **131.2** | | 170.4 |
| **Property, plant, equipment and timber** | | **1,886.0** | | 1,959.4 |
| **Goodwill** | | **72.4** | | 69.2 |
| **Deferred charges** | | **105.8** | | 90.0 |
| | **$** | **3,321.4** | $ | 3,507.8 |
| **LIABILITIES** | | | | |
| **Current Liabilities** | | | | |
| Operating bank loans (Note 9) | **$** | **4.1** | $ | - |
| Accounts payable and accrued liabilities | | **306.1** | | 335.0 |
| Current portion of long-term debt (Note 9) | | **145.5** | | 15.2 |
| Current portion of deferred reforestation obligation | | **38.3** | | 34.4 |
| Future income taxes, net | | **4.6** | | 19.0 |
| Total current liabilities | | **498.6** | | 403.6 |
| **Long-term debt** (Note 9) | | **371.3** | | 481.6 |
| **Long-term accrued liabilities and obligations** (Note 10) | | **205.2** | | 203.5 |
| **Future income taxes, net** | | **266.1** | | 299.5 |
| **Non-controlling interests** | | **299.3** | | 302.5 |
| | **$** | **1,640.5** | $ | 1,690.7 |
| **SHAREHOLDERS' EQUITY** | | | | |
| Share capital – 142,589,312 common shares outstanding | **$** | **1,124.7** | $ | 1,124.7 |
| Contributed surplus | | **31.9** | | 31.9 |
| Retained earnings | | **546.5** | | 692.5 |
| Accumulated other comprehensive loss | | **(22.2)** | | (32.0) |
| | **$** | **1,680.9** | $ | 1,817.1 |
| | **$** | **3,321.4** | $ | 3,507.8 |

Subsequent Event (Note 14)

APPROVED BY THE BOARD

R. Lane Cliff

Director, R.L. Cliff

Director, J.F. Shepard

## Canfor Corporation
## Consolidated Statements of Changes in Shareholders' Equity and Comprehensive Income (Loss)

| (millions of dollars, unaudited) | 3 months ended September 30, **2008** | 3 months ended September 30, 2007 | 9 months ended September 30, **2008** | 9 months ended September 30, 2007 |
|---|---|---|---|---|
| **Consolidated Statements of Changes in Shareholders' Equity** | | | | |
| **Share capital** | | | | |
| Balance at beginning of period | **$ 1,124.7** | $ 1,124.6 | **$ 1,124.7** | $ 1,124.3 |
| Common shares issued on exercise of stock options | **-** | 0.1 | **-** | 0.4 |
| Balance at end of period | **$ 1,124.7** | $ 1,124.7 | **$ 1,124.7** | $ 1,124.7 |
| **Contributed surplus** | | | | |
| Balance at beginning and end of period | **$ 31.9** | $ 31.9 | **$ 31.9** | $ 31.9 |
| **Retained earnings** | | | | |
| Balance at beginning of period | **$ 640.7** | 971.6 | **$ 692.5** | $ 1,068.5 |
| Implementation of financial instruments standards (Note 1 (b)) | **-** | - | **-** | (13.2) |
| Change in accounting for Canfor Pulp Limited Partnership's pension liability | **-** | - | **-** | (2.2) |
| Change in accounting for inventories (Note 1 (b)) | **-** | - | **(30.6)** | - |
| Net loss | **(94.2)** | (42.1) | **(115.4)** | (123.6) |
| Balance at end of period | **$ 546.5** | $ 929.5 | **$ 546.5** | $ 929.5 |
| **Accumulated other comprehensive loss** | | | | |
| Balance at beginning of period | **$ (27.0)** | $ (17.1) | **$ (32.0)** | $ **-** |
| Implementation of financial instruments standards (Note 1 (b)) | **-** | - | **-** | (1.9) |
| Reclassification from foreign exchange translation adjustment | **-** | - | **-** | 3.0 |
| Net change in foreign exchange translation adjustment | **5.1** | (13.4) | **10.5** | (33.8) |
| Reclassification to income of losses on derivatives designated as cash flow hedges in prior periods | **(0.3)** | 0.4 | **(0.7)** | 2.6 |
| Balance at end of period | **$ (22.2)** | $ (30.1) | **$ (22.2)** | $ (30.1) |
| **Shareholders' equity at end of period** | **$ 1,680.9** | $ 2,056.0 | **$ 1,680.9** | $ 2,056.0 |
| **Consolidated Statement of Comprehensive Income (Loss)** | | | | |
| Net loss | **$ (94.2)** | $ (42.1) | **$ (115.4)** | $ (123.6) |
| Other comprehensive income (loss) | | | | |
| Exchange translation adjustment on self-sustaining foreign subsidiaries | **5.1** | (13.4) | **10.5** | (33.8) |
| Reclassification to income of losses on derivative instruments designated as cash flow hedges in prior periods, net of taxes and non-controlling interests | **(0.3)** | 0.4 | **(0.7)** | 2.6 |
| Other comprehensive income (loss) | **4.8** | (13.0) | **9.8** | (31.2) |
| **Total comprehensive loss** | **$ (89.4)** | $ (55.1) | **$ (105.6)** | $ (154.8) |

## Notes to the Consolidated Interim Financial Statements

(unaudited, in millions of dollars unless otherwise noted)

### 1. Significant Accounting Policies and Changes in Accounting Policies

### (a) Basis of Presentation

These interim financial statements do not include all of the disclosures required by Canadian generally accepted accounting principles for annual financial statements and, accordingly, should be read in conjunction with the financial statements and notes included in Canfor's Annual Report for the year ended December 31, 2007 available at www.canfor.com or www.sedar.com. These interim financial statements follow the same accounting policies and methods of computation as used in the 2007 consolidated financial statements, except as noted below.

Canfor's financial results are impacted by seasonal factors such as weather and building activity. Adverse weather conditions can cause logging curtailments, which can affect the supply of raw materials to sawmills, plywood and OSB plants, and pulp mills. Market demand also varies seasonally to some degree. For example, building activity and repair and renovation work, which affects demand for lumber and panel products, is generally stronger in the spring and summer months. Shipment volumes are affected by these factors as well as by global supply and demand conditions.

### (b) Changes in Accounting Policies

Effective January 1, 2008, the Company adopted the Canadian Institute of Chartered Accountants' new Handbook Sections: 1535 "Capital Disclosures", 3031 "Inventories", 3862 "Financial Instruments – Disclosures" and 3863 "Financial Instruments – Presentation". Handbook sections 3862 and 3863 replace section 3861 "Financial Instruments – Disclosure and Presentation". These recommendations have been incorporated into the unaudited interim consolidated financial statements.

*Section 1535 - Capital Disclosures*

This section establishes standards for disclosures about an entity's capital and how it is managed. Under this standard the Company is required to disclose qualitative information about its objectives, policies and processes for managing capital; to disclose quantitative data about what it regards as capital; and to disclose whether an entity has complied with any externally imposed capital requirements and, if not, the consequences of such non-compliance.

*Section 3031 - Inventories*

This Section replaced Section 3030 – "Inventories" and provides significantly more guidance on the measurement of inventories, with an expanded definition of cost, and the requirement that inventories must be measured at the lower of cost and net realizable value. In addition, the section sets out additional disclosure requirements, including accounting policies, carrying values, and the amount of any inventory write-downs or reversal of write-downs. In conjunction with section 3061 "Property Plant and Equipment", it also provides guidance on the classification of major spare parts and stand-by equipment.

On January 1, 2008, the Company adopted the new recommendations on a prospective basis. As a result of implementing these standards, inventories decreased by $60.6 million (log inventories by $46.5 million, processing materials and supplies by $14.1 million), property, plant and equipment increased by $14.1 million, future income tax liabilities decreased by $15.9 million and opening retained earnings were reduced by $30.6 million.

Total log and finished product inventory write-downs at September 30, 2008 were $22.2 million.

*Section 3862 - Financial Instruments – Disclosures*

This section requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate: (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks.

*Section 3863 – Financial Instruments – Presentation*

This Section establishes standards for presentation of financial instruments and non-financial derivatives.

On January 1, 2007, the Company adopted Sections 3855, 3861, 3865, "*Financial Instruments", "Financial Instruments – Disclosure and Presentation, Hedges"* and Section 1530, "*Comprehensive Income"*. Opening retained earnings were reduced by $13.2 million as a result of the implementation of these new standards. This amount was comprised of a $14.2 million deferred unrealized foreign exchange loss on long-term debt arising from a previous hedging relationship and $2.8 million of deferred financing costs that were written off, partially offset by a $3.8 million adjustment to the associated liabilities for future income taxes and non-controlling interests.

### (c) Future Accounting Policy Changes

In 2007, the Canadian Accounting Standards Board announced that Canadian generally accepted accounting principles ("Canadian GAAP") will cease to exist for all publicly accountable enterprises targeted for fiscal years commencing January 1, 2011. From that date onward, publicly traded companies and certain other publicly accountable enterprises will be required to report under International Financial Reporting Standards ("IFRS"). The impact of the transition to IFRS on the Company's consolidated financial statements has not yet been determined.

In February 2008, the CICA issued a new accounting standard, Handbook Section 3064, Goodwill and Intangible Assets. This section replaces CICA Handbook Section 3062, Goodwill and Intangible Assets, and establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of various preproduction and start-up costs and requires that these costs be expensed as incurred. This standard will be applicable to the Company for annual and interim accounting periods beginning on January 1, 2009. The Company does not expect that this standard will have a material impact on its consolidated financial statements.

## 2. Restructuring, Mill Closure and Severance Costs

Restructuring, mill closure and severance costs of $5.4 million for the third quarter of 2008 were substantially comprised of costs resulting from the indefinite closures of the Company's PolarBoard and Mackenzie operations.

The following table provides a reconciliation of accrued amounts relating to the indefinite or permanent closures of facilities, as well as severance costs:

| (millions of dollars) | **As at September 30, 2008** | As at December 31, 2007 |
|---|---|---|
| Accrued liability at beginning of period | **$ 41.4** | $ 4.9 |
| Accrued in the period * | **5.4** | 41.3 |
| Less: non-cash items | **(0.9)** | (2.0) |
| Payments in the period | **(11.5)** | (8.4) |
| Accrued liability at end of period | **$ 34.4** | $ 35.8 |

| * reported in the following segments' income statements (millions of dollars) | **3 months ended September 30, 2008** | Year ended December 31, 2007 |
|---|---|---|
| Lumber | **$ 3.1** | $ 21.7 |
| Panels | **2.3** | 14.4 |
| Corporate and Other | **-** | 5.2 |
| | **$ 5.4** | $ 41.3 |

### 3. Employee Future Benefits

The Company's total benefit costs were as follows:

| (millions of dollars) | 3 months ended September 30, **2008** | 2007 | 9 months ended September 30, **2008** | 2007 |
|---|---|---|---|---|
| Defined benefit pension plans | **$ 0.8** | $ 3.8 | **$ 2.4** | $ 11.5 |
| Other employee future benefit plans | **4.3** | 4.4 | **12.8** | 12.9 |
| Defined contribution pension plans and 401(k) plans | **0.9** | 0.9 | **2.6** | 2.9 |
| Contributions to forest industry union plans | **4.2** | 5.6 | **14.6** | 18.2 |
| | **$ 10.2** | $ 14.7 | **$ 32.4** | $ 45.5 |

### 4. Insurance Receivable - Fires at North Central Plywoods Mill and Prince George Pulp & Paper Mill

(a) North Central Plywoods Mill Fire

On May 26, 2008 a fire at the Company's North Central Plywoods (NCP) facility in Prince George, British Columbia completely destroyed the mill. The mill is insured for equivalent replacement value. At the end of the second quarter of 2008, the Company had not reached a final settlement with its insurer, and accordingly, estimated the insurance property damage amount receivable using preliminary engineering estimates and other information then available. Based on estimated insurance proceeds, net of an aggregate policy deductible of $2.4 million, and costs related to the fire, the Company has recorded a pre-tax gain of $57.9 million and restructuring, mill closure and severance costs of $13.3 million. The estimates are subject to adjustments in future periods. On July 4, 2008, the Company received a cash advance of $10 million from its insurer.

(b) Prince George Pulp & Paper Mill Fire

On January 15, 2008, a fire at Canfor Pulp Limited Partnership's (CPLP) Prince George Pulp & Paper mill destroyed the chip screening and in-feed system. CPLP recorded a related gain on disposal of capital assets of $8.5 million in the first quarter of 2008. In connection with claims arising from the fire, CPLP has recorded the following receivables at September 30, 2008:

- a property damage insurance receivable of $12.2 million, net of an aggregate policy deductible of $3.3 million; and
- a business interruption insurance receivable of $18.1 million, which has been credited to sales in the applicable quarters.

By September 30, 2008, CPLP had received total advances of $22.9 million in connection with these claims, of which $13.4 million related to the business interruption claim, and $9.5 million related to property damage. Of the latter amount, $8.0 million has been classified as an investing activity in the consolidated cash flow statement; the balance of $1.5 million represents demolition costs.

### 5. Income Tax (Expense) Recovery

| (millions of dollars) | 3 months ended September 30, **2008** | 2007 | 9 months ended September 30, **2008** | 2007 |
|---|---|---|---|---|
| Current | **$ 17.2** | $ 37.5 | **$ 29.9** | $ 77.9 |
| Future | **12.8** | (10.3) | **31.8** | 0.9 |
| | **$ 30.0** | $ 27.2 | **$ 61.7** | $ 78.8 |

The reconciliation of income taxes calculated at the statutory rate to the actual income tax provision is as follows:

| (millions of dollars) | 3 months ended September 30, 2008 | 2007 | 9 months ended September 30, 2008 | 2007 |
|---|---|---|---|---|
| Income tax recovery at statutory tax rate | **$ 36.8** | $ 17.8 | **$ 43.5** | $ 48.8 |
| Add (deduct): | | | | |
| Non-controlling interests | **1.6** | 5.7 | **11.3** | 20.2 |
| Change in corporate income tax rate | **-** | 0.9 | **9.1** | 1.9 |
| Entities with different income tax rates and other tax adjustments | **1.8** | 2.9 | **3.5** | 5.8 |
| Tax recovery at rates other than statutory rate | **2.2** | - | **2.6** | - |
| Permanent difference from capital gains and losses and other non-deductible items | **(12.4)** | (0.1) | **(8.3)** | 2.1 |
| Income tax recovery | **$ 30.0** | $ 27.2 | **$ 61.7** | $ 78.8 |

## 6. Net Income (Loss) Per Share

Basic net income (loss) per share is calculated by dividing the net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is calculated by dividing the net income (loss) available to common shareholders by the weighted average number of common shares during the period using the treasury stock method. Under this method, proceeds from the potential exercise of stock options are assumed to be used to purchase the Company's common shares. When there is a net loss, the exercise of stock options would result in a calculated diluted net loss per share that is anti-dilutive.

| | 3 months ended September 30, 2008 | 2007 | 9 months ended September 30, 2008 | 2007 |
|---|---|---|---|---|
| Weighted average number of common shares | **142,589,312** | 142,583,682 | **142,589,312** | 142,571,876 |
| Incremental shares from potential exercise of options (Note) | **3,419** | 53,905 | **2,371** | 53,889 |
| Diluted number of common shares (Note) | **142,589,312** | 142,583,682 | **142,589,312** | 142,571,876 |

Note: Where the addition of share options to the total shares outstanding has an anti-dilutive impact on the diluted net income (loss) per share calculation, those share options have not been included in the total common shares outstanding for purposes of the calculation of diluted net income (loss) per share.

## 7. Changes in Non-Cash Working Capital

| (millions of dollars) | 3 months ended September 30, 2008 | 2007 | 9 months ended September 30, 2008 | 2007 |
|---|---|---|---|---|
| Accounts receivable | **$ 14.0** | $ 29.2 | **$ (2.9)** | $ 3.6 |
| Income taxes | **(4.7)** | (25.5) | **107.7** | (308.2) |
| Future income taxes | **4.1** | 7.3 | **(27.4)** | (3.6) |
| Inventories | **(3.0)** | 70.5 | **(11.0)** | 120.9 |
| Prepaid expenses | **5.2** | 4.0 | **(14.9)** | (9.4) |
| Accounts payable, accrued liabilities and current portion of deferred reforestation | **(12.9)** | 35.9 | **(5.6)** | (222.1) |
| | **$ 2.7** | $ 121.4 | **$ 45.9** | $ (418.8) |

## 8. Long-Term Investments and Other

(a) Asset-Backed Commercial Paper

Long-term investments and other includes US$64.0 million for non-bank asset-backed commercial paper (ABCP). The ABCP is measured at the estimated fair value of combined investments in asset-backed commercial paper of four different Canadian trusts (the Trusts) with total original principal amount of US$81.2 million and original maturities between August and September 2007. At the dates the Company acquired these investments they were rated R1 (High) by Dominion Bond Rating Service (DBRS), the highest credit rating issued for commercial paper and backed by R1 (High) rated assets and liquidity arrangements.

Since August of 2007, the market for ABCP has experienced significant liquidity problems. The demand for such paper has disappeared following the decline in credit markets and concerns regarding the quality and nature of underlying assets. The Trusts failed to make payment at maturity and, along with 16 other ABCP conduits, are subject to restructuring under the Pan-Canadian Investors Committee for Third Party structured Asset-Backed Commercial Paper (the Pan-Canadian Investors Committee).

On March 17, 2008 the Pan-Canadian Investors Committee filed with the Ontario Superior Court of Justice (the Court) a comprehensive arrangement pursuant to the Companies' Creditors Arrangement Act (CCAA) to restructure the affected trusts. On April 25, noteholders voted overwhelmingly in favour of the restructuring plan. On June 5, 2008, the Court approved the Pan Canadian Investors Committee plan to restructure the 20 ABCP conduits. Following an unsuccessful appeal by certain investors to the Ontario Court of Appeal, the Supreme Court of Canada on September 19 denied the plaintiffs further leave to appeal. The restructuring is currently expected to be completed by the end of 2008.

Due to the disruption in the ABCP market, quoted market values of the investments have not been available. Therefore, the fair value of the ABCP has been determined based on management's judgment using all currently available information and estimated assumptions that market participants would use in pricing such ABCP as at the balance sheet date. In estimating fair value, Canfor used a valuation approach based on a high likelihood of successful restructuring of the investment. Of the US$81.2 million of ABCP which the Company has invested, it is estimated that:

- US$4.3 million is represented by traditional securitized assets that will, on restructuring, be replaced with long-term floating rate notes that are expected to receive a high investment grade rating;
- US$18.2 million is represented by a combination of synthetic and traditional securitized assets and collateralized debt obligations that will, on restructuring, be pooled with similar assets from other trusts and be replaced with a mix of senior and subordinated floating rate notes. It is anticipated that approximately 90% of the notes received by the Company will be senior notes and will carry a high investment grade rating;
- US$21.0 million is represented by assets that have exposure to US sub-prime assets or home equity loan mortgages that will, on restructuring, be replaced with long-term floating rate notes that may or may not be rated; and
- US$37.5 million is represented by assets of the Ironstone Trust Series B that had a rating of AAA by DBRS, published on January 9, 2008 (subsequently downgraded to 'D' on CCAA filing). On restructuring, the assets will be replaced with a long-term floating rate note that may or may not be rated.

It is possible that further information will become available on the actual composition of the referenced assets. A change in the estimate of the composition of the referenced assets would affect the valuation. In addition, if sales of the restructured senior or subordinated notes occur in the future, these sales might represent observable market transactions that could appropriately be used to determine the fair value of the investment.

(b) Asset Impairments

In the third quarter of 2008, the Company recorded an asset impairment charge of $70.0 million related to investments in Howe Sound Pulp and Paper Limited Partnership (HSLP), which reflected current fair value, based on estimated future cash flows. The Company's investments include a 50% interest in Coastal Fibre Limited Partnership (CFLP), an entity which supplies fibre and related services to HSLP. The impairment reflects the continuing deterioration of B.C. Coastal pulp, paper and fibre market conditions. The affected assets are included in the 'Corporate & Other' reporting segment.

## 9. Operating Bank Loan and Long-Term Debt

In July 2008, Canfor Corporation increased its operating line of credit by $30.0 million to $355.0 million. At September 30, 2008, the Company, on a consolidated basis, had $439.0 million of bank operating lines of credit available, of which $4.1 million was drawn down and an additional $44.5 million was reserved for several standby letters of credit.

At September 30, 2008, the fair value of the Company's long-term debt, which was measured at its amortized cost of $516.8 million, was $518.0 million. The fair value of long-term debt was determined based on prevailing market rates for long-term debt with similar characteristics and risk profiles.

## 10. Long-term Accrued Liabilities and Obligations

| (millions of dollars) | **As at September 30, 2008** | As at December 31, 2007 |
|---|---|---|
| Deferred reforestation obligation | **$ 55.9** | $ 65.6 |
| Accrued pension obligations | **20.5** | 19.1 |
| Accrued pension bridge benefit obligations | **8.7** | 7.9 |
| Post employment benefits | **95.7** | 87.0 |
| Asset retirement obligations | **11.4** | 11.1 |
| Other long-term liabilities | **13.0** | 12.8 |
| | **$ 205.2** | $ 203.5 |

## 11. Segmented Information [a]

Business Segment Information

| (millions of dollars) | | Lumber [b] | Panels | Pulp & Paper [d] | Corporate & Other | | Consolidated |
|---|---|---|---|---|---|---|---|
| **3 months ended September 30, 2008** | | | | | | | |
| **Sales to external customers** | **$** | **378.8** | **36.0** | **253.2** | **-** | **$** | **668.0** |
| **Sales to other segments [c]** | **$** | **22.7** | **0.5** | **-** | **-** | **$** | **23.2** |
| **Operating income (loss)** | **$** | **(8.2)** | **(3.4)** | **31.5** | **(7.1)** | **$** | **12.8** |
| **Amortization** | **$** | **23.4** | **3.3** | **13.6** | **1.9** | **$** | **42.2** |
| **Capital expenditures** | **$** | **14.1** | **0.3** | **7.8** | **-** | **$** | **22.2** |
| 3 months ended September 30, 2007 | | | | | | | |
| Sales to external customers | $ | 507.2 | 73.9 | 256.3 | - | $ | 837.4 |
| Sales to other segments [c] | $ | 30.0 | 1.5 | - | - | $ | 31.5 |
| Operating income (loss) | $ | (75.9) | (7.5) | 36.1 | (4.8) | $ | (52.1) |
| Amortization | $ | 25.4 | 5.5 | 13.6 | 1.1 | $ | 45.6 |
| Capital expenditures | $ | 15.3 | 2.2 | 4.6 | 1.6 | $ | 23.7 |
| **9 months ended September 30, 2008** | | | | | | | |
| **Sales to external customers** | **$** | **1,126.6** | **149.8** | **746.5** | **-** | **$** | **2,022.9** |
| **Sales to other segments [c]** | **$** | **73.3** | **3.2** | **-** | **-** | **$** | **76.5** |
| **Operating income (loss)** | **$** | **(104.2)** | **(41.7)** | **79.0** | **(17.0)** | **$** | **(83.9)** |
| **Amortization** | **$** | **72.7** | **11.8** | **37.7** | **5.0** | **$** | **127.2** |
| **Capital expenditures** | **$** | **30.7** | **0.7** | **26.9** | **-** | **$** | **58.3** |
| **Identifiable assets [e]** | **$** | **1,510.7** | **332.1** | **941.5** | **537.1** | **$** | **3,321.4** |
| 9 months ended September 30, 2007 | | | | | | | |
| Sales to external customers | $ | 1,547.4 | 227.2 | 790.0 | - | $ | 2,564.6 |
| Sales to other segments [c] | $ | 88.8 | 3.6 | - | - | $ | 92.4 |
| Operating income (loss) | $ | (201.7) | (42.3) | 124.3 | (28.6) | $ | (148.3) |
| Amortization | $ | 77.2 | 17.6 | 38.5 | 3.6 | $ | 136.9 |
| Capital expenditures | $ | 41.9 | 5.7 | 12.9 | 2.6 | $ | 63.1 |
| Identifiable assets [e] | $ | 1,767.5 | 435.3 | 976.7 | 714.1 | $ | 3,893.6 |

(a) Operations are presented by product line.

(b) Sales for the third quarter include sales of Canfor-produced lumber of $300.8 million (three months ended September 30, 2007 – $430.8 million) and $916.4 million for the year-to-date (nine months ended September 30, 2007 – $1,305.2 million).

(c) Sales to other segments are accounted for at prices that approximate market value.

(d) Includes 100% of Canfor Pulp Limited Partnership and the Taylor Pulp Mill, which was excluded from the spinout of the pulp and paper business in 2006.

(e) Identifiable assets of the Lumber segment includes goodwill of $72.4 million (September 30, 2007 - $69.7 million), which resulted from the acquisition of New South Companies Inc. in March 2006.

Geographic Information

| (millions of dollars) | 3 months ended September 30, 2008 | 2007 | 9 months ended September 30, 2008 | 2007 |
|---|---|---|---|---|
| Sales by location of customer | | | | |
| Canada | **$ 132.9** | $ 165.5 | **$ 395.9** | $ 466.3 |
| United States | **341.5** | 466.3 | **1,060.7** | 1,489.0 |
| Europe | **40.9** | 52.6 | **137.2** | 140.3 |
| Far East and Other | **152.7** | 153.0 | **429.1** | 469.0 |
| | **$ 668.0** | $ 837.4 | **$ 2,022.9** | $ 2,564.6 |

| (millions of dollars) | **As at September 30, 2008** | As at December 31, 2007 |
|---|---|---|
| Capital assets and goodwill by location | | |
| Canada | **$ 1,799.6** | $ 1,868.9 |
| United States | **157.9** | 158.8 |
| Far East and Other | **0.9** | 0.9 |
| | **$ 1,958.4** | $ 2,028.6 |

## 12. Financial Instruments

All financial instruments and derivatives are measured at fair value on initial recognition except for certain related party transactions.

*Classification of Financial Instruments*

The Company has classified its cash and cash equivalents and ABCP as held-for-trading. Accounts receivable are classified as loans and receivables. Bank indebtedness, accounts payable and accrued charges, and long-term debt, including interest payable, are classified as other liabilities, all of which are measured at amortized cost. Derivative instruments are recorded at fair value, including those derivatives that are embedded in financial or non-financial contracts that are not closely related to the host contract.

*Financial Risk Management*

The Company is exposed to a number of risks as a result of holding financial instruments. These risks include credit risk, liquidity risk and market price risk.

The Company's Risk Management Committee manages risk in accordance with a Board approved Price Risk Management Controls Policy. This policy provides the framework for risk management related to commodity price, foreign exchange, interest rate and counterparty credit risk of the Company.

*I. Credit risk:*

Credit risk is the risk of financial loss to the Company if a customer or third party to a derivative instrument fails to meet its contractual obligations.

Financial instruments that are subject to credit risk include cash and cash equivalents, accounts receivable and long-term investments and other. Cash and cash equivalents includes cash held through major Canadian and international financial institutions and temporary investments with an original maturity date of 90 days or less. The cash and cash equivalents balance at September 30, 2008 is $334.2 million.

The Company utilizes a combination of credit insurance and self-insurance to manage the risk associated with trade receivables. Approximately 50% of the outstanding trade receivables are covered by credit insurance and the remaining balances are with creditworthy counterparties. The Company's trade receivable balance at September 30, 2008 is $202.6 million.

*II. Liquidity risk:*

Liquidity risk is the risk that the Company will be unable to meet its financial obligations on a current basis. The Company manages liquidity risk through regular cash-flow forecasting in conjunction with an adequate committed operating bank loan facility.

At September 30, 2008, the Company has accounts payable and accrued liabilities of $306.1 million and current debt obligations of $145.5 million (US$137.3 million), all of which fall due for payment within one year of the balance sheet date.

*III. Market risk:*

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in interest rates and foreign currency.

a. Interest Rate risk:

The Company is exposed to interest rate risk through its current financial assets and financial obligations bearing variable interest rate. The Company's cash and cash equivalents include term deposits with original maturity dates of 90 days or less.

Changes in the market interest rates do not have a significant impact on the Company's results of operations due to the short-term nature of the respective financial assets and obligations and because all long-term debt is based on fixed rates of interest.

The Company currently does not use derivative instruments to reduce its exposure to interest rate risk.

b. Currency risk:

The Company is exposed to foreign exchange risk primarily related to the U.S. dollar, as the Company's products are sold principally in U.S. dollars and all long term debt is denominated in U.S. dollars. In addition, the Company holds financial assets and liabilities primarily related to New South Companies Inc. based in South Carolina, in U.S. dollars.

A portion of the currency risk associated with U.S. dollar denominated sales is naturally offset by U.S. dollar denominated expenses and the U.S. dollar denominated debt. The majority of the remaining exposure is subject to option contracts (foreign exchange collars) that effectively limit the minimum and maximum Canadian dollar recovery related to the sale of those dollars.

c. Energy Price risk

The Company is exposed to energy price risk relating to purchases of natural gas and diesel oil for use in its operations.

The exposure is hedged up to 100% through the use of floating to fixed swap contracts or option contracts with maturity dates up to a maximum of three years.

d. Commodity Price risk

The Company is exposed to commodity price risk related to sale of lumber, pulp, paper, plywood and oriented strand board. From time to time, the Company will enter into futures contracts on the Chicago Mercantile Exchange for lumber and forward contracts direct with customers for pulp. Under the Price Risk Management Controls Policy, up to 15% of lumber sales and 5% of pulp sales may be sold in this way.

*Derivative Instruments*

The Company uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, lumber prices and energy costs. At September 30, 2008, the fair value of outstanding commodity and exchange contracts was a net liability of $6.9 million. The fair value of these contracts was determined based on prevailing market rates for instruments with similar characteristics.

A loss on derivative financial instruments of $38.8 million was recorded in the third quarter, which comprised realized gains of $1.2 million, unrealized mark to market losses of $40.4 million and the reclassification, from accumulated other comprehensive income, of unrealized gains of $0.4 million formerly designated as cash flow hedges, which were exercised in the current period.

Gain (Loss) on Derivative Financial Instruments

| | 3 months ended September 30, | | 9 months ended September 30, | |
|---|---|---|---|---|
| (millions of dollars) | **2008** | 2007 | **2008** | 2007 |
| Natural gas swaps | **$ (25.3)** | $ (6.1) | **$ 5.8** | $ (10.2) |
| Diesel options and swaps | **(3.5)** | 0.2 | **8.0** | 4.9 |
| Foreign exchange collars | **(9.4)** | 15.2 | **(20.6)** | 15.1 |
| Lumber futures | **(0.6)** | (0.4) | **-** | - |
| | **$ (38.8)** | $ 8.9 | **$ (6.8)** | $ 9.8 |

## 13. Capital Disclosures

The Company's objectives when managing capital are to safeguard its assets and maintain a globally competitive cost structure while looking for growth opportunities to ensure the ability to continue as a going concern and provide adequate returns to shareholders. In addition, the Company works with all relevant stakeholders to ensure the safety of its operations and employees meet and exceed all environmental regulations.

The Company's capital is comprised of net debt and shareholders' equity:

| (millions of dollars) | **As at September 30, 2008** | As at December 31, 2007 |
|---|---|---|
| Total debt (including operating bank loans) | **$ 520.9** | $ 496.8 |
| Less: Cash and cash equivalents | **(334.2)** | (295.5) |
| Net debt | **186.7** | 201.3 |
| Total shareholders' equity | **1,680.9** | 1,817.1 |
| | **$ 1,867.6** | $ 2,018.4 |

For the three and nine months ended September 30, 2008, the Company remained in compliance with all covenants related to its debt facilities.

## 14. Subsequent Event

In October 2008, the Company announced the indefinite closure of the Tackama plywood plant in Fort Nelson, British Columbia, as a result of weak plywood demand and prices. The Company anticipates that restructuring, mill closure and severance costs of approximately $5 million will be recorded in the last quarter of 2008.

## 15. Comparative Figures

Certain comparative information has been reclassified to conform to the presentation in the current period.