2018

CANFOR PULP PRODUCTS INC.

FINANCIAL STATEMENTS

MANAGEMENT'S RESPONSIBILITY

The information and representations in these consolidated financial statements are the responsibility of management and have been approved by the Board of Directors. The consolidated financial statements were prepared by management in accordance with International Financial Reporting Standards and, where necessary, reflect management's best estimates and judgments at this time. It is reasonably possible that circumstances may arise which cause actual results to differ.

Canfor Pulp Products Inc. maintains systems of internal controls over financial reporting, policies and procedures to provide reasonable assurance as to the reliability of the financial records and the safeguarding of its assets.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board carries out these activities primarily through its Audit Committee.

The Audit Committee is comprised of three Directors who are not employees of the Company. The Audit Committee meets periodically throughout the year with management, external auditors and internal auditors to review their respective responsibilities, results of the reviews of internal controls over financial reporting, policies and procedures and financial reporting matters. The external and internal auditors meet separately with the Audit Committee.

The consolidated financial statements have been reviewed by the Audit Committee and approved by the Board of Directors. The consolidated financial statements have been audited by KPMG LLP, the external auditors, whose report follows.

February 21, 2019

"*Don B. Kayne*" "*Alan Nicholl*"

Don B. Kayne
Chief Executive Officer

Alan Nicholl
Chief Financial Officer

KPMG LLP
PO Box 10426 777 Dunsmuir Street
Vancouver BC V7Y 1K3
Canada
Telephone (604) 691-3000
Fax (604) 691-3031

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Canfor Pulp Products Inc.

Opinion

We have audited the consolidated financial statements of Canfor Pulp Products Inc. (the "Company"), which comprise:

- the consolidated balance sheets as at December 31, 2018 and December 31, 2017;
- the consolidated statements of income for the years then ended;
- the consolidated statements of comprehensive income for the years then ended;
- the consolidated statements of changes in equity for the years then ended;
- the consolidated statements of cash flows for the years then ended; and,
- notes to the consolidated financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2018 and December 31, 2017, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the **"*Auditors' Responsibilities for the Audit of the Financial Statements*"** section of our auditors' report.

We are independent of the Company in accordance with the ethical requirements that are relevant to or audit of the financial statements in Canada and we have fulfilled our other responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

KPMG

Other Information

Management is responsible for the other information. Other information comprises:

– the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions.
– the information, other than the financial statements and the auditors' report thereon, included in the "2018 Canfor Pulp Products Inc. Annual Report".

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We obtained Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions as at the date of this auditors' report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors' report.

We have nothing to report in this regard.

The 2018 Canfor Pulp Products Inc. Annual Report is expected to be made available to us after the date of this auditors' report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance for the financial statements.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance for the financial statements are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Communicate with those charged with governance for the financial statements regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

- Provide those charged with governance for the financial statements with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

KPMG LLP

Chartered Professional Accountants

The engagement partner on the audit resulting in this auditors' report is John Desjardins.

Vancouver, Canada
February 21, 2019

Canfor Pulp Products Inc.
Consolidated Balance Sheets

(millions of Canadian dollars)		**As at December 31, 2018**		As at December 31, 2017
ASSETS				
Current assets				
Cash and cash equivalents	**$**	**6.9**	$	76.7
Accounts receivable - Trade		**107.6**		101.5
- Other		**11.4**		14.3
Income taxes receivable		**5.4**		-
Inventories (Note 6)		**207.1**		165.5
Prepaid expenses		**11.9**		7.0
Total current assets		**350.3**		365.0
Property, plant and equipment and intangible assets (Note 7)		**578.2**		526.7
Other long-term assets		**3.5**		0.5
Total assets	**$**	**932.0**	$	892.2
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities (Note 8)	**$**	**182.0**	$	161.5
Total current liabilities		**182.0**		161.5
Retirement benefit obligations (Note 11)		**80.0**		85.2
Other long-term provisions		**6.6**		6.5
Deferred income taxes, net (Note 15)		**66.8**		67.6
Total liabilities	**$**	**335.4**	$	320.8
EQUITY				
Share capital (Note 13)	**$**	**480.9**	$	480.9
Retained earnings		**115.7**		90.5
Total equity	**$**	**596.6**	$	571.4
Total liabilities and equity	**$**	**932.0**	$	892.2

Commitments and Contingencies (Note 19) and **Subsequent Event** (Note 24)

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

APPROVED BY THE BOARD

"S.E. Bracken-Horrocks"

Director, S.E. Bracken-Horrocks

"C.A. Pinette"

Director, C.A. Pinette

Canfor Pulp Products Inc.
Consolidated Statements of Income

(millions of Canadian dollars, except per share data)		Years ended December 31, **2018**		2017
Sales	**$**	**1,374.3**	$	1,197.9
Costs and expenses				
Manufacturing and product costs		**870.9**		786.7
Freight and other distribution costs		**145.4**		155.0
Amortization		**79.6**		74.4
Selling and administration costs		**31.8**		27.2
		1,127.7		1,043.3
Operating income		**246.6**		154.6
Finance expense, net (Note 14)		**(4.2)**		(7.2)
Other income (expense), net		**8.7**		(6.5)
Net income before income taxes		**251.1**		140.9
Income tax expense (Note 15)		**(66.7)**		(38.8)
Net income	**$**	**184.4**	$	102.1
Net income per common share: (in Canadian dollars)				
Attributable to equity shareholders of the Company				
- Basic and diluted (Note 13)	**$**	**2.83**	$	1.55

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

Canfor Pulp Products Inc.
Consolidated Statements of Other Comprehensive Income

(millions of Canadian dollars)	Years ended December 31, **2018**	2017
Net income	**$ 184.4**	$ 102.1
Other comprehensive income		
Items that will not be recycled through net income:		
Defined benefit plan actuarial gains (Note 11)	**5.5**	25.2
Income tax expense on defined benefit plan actuarial gains (Note 15)	**(1.5)**	(6.3)
Other comprehensive income, net of tax	**4.0**	18.9
Total comprehensive income	**$ 188.4**	$ 121.0

Consolidated Statements of Changes in Equity

(millions of Canadian dollars)	Years ended December 31, **2018**	2017
Share capital		
Balance at beginning of year	**$ 480.9**	$ 491.6
Share purchases (Note 13)	**-**	(10.7)
Balance at end of year (Note 13)	**$ 480.9**	$ 480.9
Retained earnings (deficit)		
Balance at beginning of year	**$ 90.5**	$ (6.9)
Net income	**184.4**	102.1
Defined benefit plan actuarial gains, net of tax	**4.0**	18.9
Dividends declared (Note 23)	**(163.2)**	(16.5)
Share purchases (Note 13)	**-**	(7.1)
Balance at end of year	**$ 115.7**	$ 90.5
Total equity	**$ 596.6**	$ 571.4

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

Canfor Pulp Products Inc.
Consolidated Statements of Cash Flows

(millions of Canadian dollars)	Years ended December 31, 2018	2017
Cash generated from (used in):		
Operating activities		
Net income	**$ 184.4**	$ 102.1
Items not affecting cash:		
Amortization	**79.6**	74.4
Income tax expense	**66.7**	38.8
Employee future benefits	**4.0**	4.3
Finance expense, net	**4.2**	7.2
Other, net	**(1.1)**	0.4
Defined benefit plan contributions	**(6.6)**	(7.0)
Income taxes paid, net	**(90.4)**	(19.1)
	240.8	201.1
Net change in non-cash working capital (Note 16)	**(25.6)**	(6.4)
	215.2	194.7
Financing activities		
Repayment of long-term debt (Note 10)	**-**	(50.0)
Finance expenses paid	**(3.3)**	(3.3)
Dividends paid (Note 23)	**(163.2)**	(16.5)
Share purchases (Note 13)	**(0.1)**	(17.7)
	(166.6)	(87.5)
Investing activities		
Additions to property, plant and equipment and intangible assets, net (Note 7)	**(120.5)**	(83.1)
Other, net	**2.1**	0.7
	(118.4)	(82.4)
Increase (decrease) in cash and cash equivalents*	**(69.8)**	24.8
Cash and cash equivalents at beginning of year*	**76.7**	51.9
Cash and cash equivalents at end of year*	**$ 6.9**	$ 76.7

*Cash and cash equivalents include cash on hand less unpresented cheques.

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

1. Reporting Entity

Canfor Pulp Products Inc. ("CPPI") is a company incorporated and domiciled in Canada and listed on The Toronto Stock Exchange. The address of the Company's registered office is 100-1700 West 75th Avenue, Vancouver, British Columbia, Canada, V6P 6G2. The consolidated financial statements of the Company as at and for the year ended December 31, 2018 comprise the Company and its subsidiaries (together referred to as "CPPI" or "the Company"). The Company's operations consist of two Northern Bleached Softwood Kraft ("NBSK") pulp mills and one NBSK pulp and paper mill located in Prince George, British Columbia, a Bleached Chemi-Thermo Mechanical Pulp ("BCTMP") mill located in Taylor, British Columbia and a marketing group based in Vancouver, British Columbia.

At December 31, 2018, and February 21, 2019, Canfor Corporation ("Canfor") held a 54.8% interest in CPPI, unchanged from December 31, 2017.

2. Basis of Preparation

Statement of compliance

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

The consolidated financial statements were authorized for issue by the Board of Directors on February 21, 2019.

Basis of measurement

The consolidated financial statements have been prepared on a historical cost basis, except for the following material items:

- Financial instruments classified as measured at fair value;
- Asset retirement obligations are measured at the discounted value of expected future cash flows; and
- The retirement benefit surplus and obligation related to the defined benefit pension plans are net of the accrued benefit obligation and the fair value of the plan assets.

Use of estimates and judgments

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

The Company regularly reviews its estimates and assumptions; however, it is possible that circumstances may arise which may cause actual results to differ from management's estimates. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about the significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the applicable notes:

- Note 7 – Property, Plant and Equipment and Intangible Assets;
- Note 11 – Employee Future Benefits;
- Note 12 – Asset Retirement Obligations; and
- Note 15 – Income Taxes.

Certain comparative amounts for the prior year have been reclassified to conform to the current year's presentation.

3. Significant Accounting Policies

The following accounting policies have been applied to the financial information presented.

Basis of consolidation

Subsidiaries are entities controlled by the Company. Control exists when CPPI is able to govern the financial and operating activities of those other entities to generate returns for the Company. Inter-company transactions, balances and unrealized gains and losses on transactions between different entities within the Company are eliminated.

For joint operations, the Company recognizes its assets, liabilities and transactions, including its share of those incurred jointly, in its consolidated financial statements.

Cash and cash equivalents

Cash and cash equivalents include cash in bank accounts and liquid money market instruments with original maturities, or redemption dates, of three months or less from the date of acquisition, and are valued at amortized cost, which approximates market value. Cash is presented net of unpresented cheques. When the amount of unpresented cheques is greater than the amount of cash, the net amount is presented as cheques issued in excess of cash on hand. Interest is earned at variable rates dependent on amount, credit quality and term of the Company's deposits.

Financial Instruments

Financial instruments comprise cash and cash equivalents, trade and other accounts receivables, accounts payable and accrued liabilities and operating loans. From time to time, CPPI uses derivative financial instruments in the normal course of its operations as a means to manage its foreign exchange, interest rate, commodity price, and energy price risk. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes. When applicable, CPPI's derivative financial instruments are not designated as hedges for accounting purposes.

CPPI's financial instruments are classified and measured as follows:

Financial Assets:	
Cash and cash equivalents	Amortized cost
Trade and other accounts receivables	Amortized cost
Financial Liabilities:	
Accounts payable and accrued liabilities	Amortized cost
Operating loans	Amortized cost

Classification and measurement of financial assets

Financial assets are classified as either measured at amortized cost, fair value through other comprehensive income ("FVOCI"), or fair value through net income ("FVTPL") based on the business model in which a financial asset is managed, its contractual cash flow characteristics and when certain conditions are met:

- Amortized cost – measured at amortized cost using the effective interest rate method. Where applicable, amortized cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairments are recognized in net income.
- FVOCI – measured at FVOCI if not designated as FVTPL. Interest income, foreign exchange gains and losses and impairments are recognized in net income. Other net gains and losses are recognized in other comprehensive income ("OCI"). On derecognition, gains and losses accumulated in OCI are reclassified to net income.
- FVTPL – measured at FVTPL if not classified as amortized cost or FVOCI with net gains and losses, including any interest or dividend income, recognized in net income.

Equity investments are required to be classified as measured at fair value. However, on initial recognition of an equity investment that is not held-for-trading, the Company may irrevocably elect to present subsequent changes in the investments fair value in OCI. This election is made on an investment by investment basis. The Company does not currently hold any equity investments.

Classification and measurement of financial liabilities

Financial liabilities are classified as either measured at amortized cost or FVTPL. A financial liability is classified as FVTPL if it is held-for-trading, a derivative or it is designated such on initial recognition. Financial liabilities at FVTPL are measured at fair value with net gains and losses, including interest expense, recognized in net income. Other financial liabilities are subsequently measured at amortized cost using the effective interest rate method. Interest expense and foreign exchange gains and losses are recognized in net income. Any gains or losses on derecognition are also recognized in net income.

Impairment

The Company applies the simplified approach in determining expected credit losses ("ECLs"), which requires a probability-weighted estimate of expected lifetime credit losses to be recognized upon initial recognition of financial assets measured at amortized cost and contract assets. Credit losses are measured as the present value of cash shortfalls from all possible default events, discounted at the effective interest rate of the financial asset. Loss allowances for financial assets at amortized cost are deducted from the gross carrying amount of the assets.

Inventories

Inventories include pulp, paper, wood chips, logs, and materials and supplies. These are measured at the lower of cost and net realizable value, and are presented net of applicable write-downs. The cost of inventories is based on the weighted average cost principle, and includes raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses.

Property, plant and equipment

Items of property, plant and equipment, including expenditure on major overhauls, are measured at cost less accumulated amortization and impairment losses.

Cost includes expenditures which are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, borrowing costs (as applicable), and any other costs directly attributable to bringing assets to the location and condition necessary for it to be used in the manner intended by management.

Expenditure on major overhauls, refits or repairs is capitalized where it enhances the life or performance of an asset above its originally assessed standard of performance. Certain expenditures relating to replacement of components incurred during major maintenance are capitalized and amortized over the estimated benefit period of such expenditures. The costs of the day-to-day servicing of property, plant and equipment are recognized in net income as incurred.

The cost of replacing a major component of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to CPPI and its cost can be measured reliably. The carrying amount of the replaced component is removed.

Amortization is recognized in net income on a straight-line basis over the estimated useful lives of each component of an item of property, plant and equipment, as set out in the table below. Land is not amortized. The majority of CPPI's amortization expense for property, plant and equipment relates to manufacturing and product costs.

Amortization methods, useful lives and residual values are reviewed, and adjusted if appropriate, at each reporting date. The following rates have been applied to CPPI's capital assets:

Buildings, roads and paving	10 to 40 years
Pulp and paper machinery and equipment	8 to 20 years
Mobile equipment	4 years
Office furniture and equipment	10 years
Major overhauls	1 to 5 years

Intangible assets

Computer software

Software development costs relate to major software systems purchased or developed by the Company. These costs are amortized on a straight-line basis over periods of four to ten years.

Government assistance

Government assistance relating to the acquisition of property, plant and equipment is recorded as a reduction of the cost of the asset to which it relates, with any amortization calculated on the net amount. Government grants related to income are recognized as income or a reimbursement of costs on a systematic basis over the periods necessary to match them with the related costs which they were intended to compensate.

Asset impairment

CPPI's property, plant and equipment and intangible assets are reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognized in net income at the amount the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows that are largely independent of cash inflows from other assets or groups of assets (cash-generating unit or "CGU").

Non-financial assets, for which impairment was recorded in a prior period, are reviewed for possible reversal of the impairment at each reporting date. When an impairment loss is reversed, the increased carrying amount of the asset cannot exceed the carrying amount that would have been determined (net of amortization) had no impairment loss been recognized in prior years.

Employee future benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity makes contributions to a separate entity and has no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution plans are recognized as an employee future benefits expense when they are earned.

For hourly employees covered by forest industry union defined contribution or benefit plans, the statement of income is charged with CPPI's contributions required under the collective agreements.

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. CPPI, in participation with Canfor, has defined benefit plans that provide both pension and other non-pension post-retirement benefits to certain salaried employees, and certain hourly employees not covered by forest industry union plans. The other non-pension post-retirement benefits include certain health care benefits and pension bridging benefits to eligible retired employees.

The surplus and/or obligation recognized in the balance sheet in respect of a defined benefit pension plan is the net of the accrued benefit obligation and the fair value of the plan assets. The accrued benefit obligation, the related service cost and, where applicable, the past service cost is determined separately for each defined benefit pension plan based on actuarial determinations using the projected unit credit method. Under the projected unit credit method, the accrued benefit obligation is calculated as the present value of each member's prospective benefits earned in respect of credited service prior to the valuation date and the related service cost is calculated as the present value of the benefits the member is assumed to earn for credited service in the ensuing year. The actuarial assumptions used in these calculations, such as salary escalation and health care inflation, are based upon best estimates selected by CPPI. The discount rate assumptions are based on the yield at the reporting date on high quality corporate bonds that have maturity dates approximating the terms of CPPI's obligations.

Actuarial gains and losses can arise from differences between actual and expected outcomes or changes in the actuarial assumptions or legislated amounts payable. Actuarial gains and losses, including the return on plan assets, are recognized in other comprehensive income in the period in which they occur.

Provisions

CPPI recognizes a provision if, as a result of a past event, it has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. The provision recorded is management’s best estimate of the expenditure required to settle the present obligation at the end of the reporting period. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The expense arising from the unwinding of the discount due to the passage of time is recorded as a finance expense. The main class of provision recognized by CPPI is as follows:

Asset retirement obligations

CPPI recognizes a liability for asset retirement obligations in the period in which they are incurred. The site restoration costs are capitalized as part of the cost of the related item of property, plant and equipment and amortized on a basis consistent with the expected useful life of the related asset. Asset retirement obligations are discounted at the risk-free rate in effect at the balance sheet date.

Revenue recognition

CPPI’s revenues are derived from the sale of pulp, paper, and energy. Revenue is measured based on the consideration specified in a contract with a customer, net of applicable sales taxes, returns, rebates and discounts and after eliminating sales within the Company. Revenue for pulp and paper is recognized when control of products is transferred to customers. Energy revenue is recognized at month-end based on energy produced and transferred to the customer under the terms and conditions of electricity purchase and load displacement agreements.

The timing of transfer of control to customers varies depending on the individual terms of the contract of sale, but is typically at the time pulp and paper is loaded onto a truck or rail carrier, upon vessel departure, or when pulp and kraft paper has been picked up by the buyer at a designated transfer point at the Company’s mill or warehouse. The amount of revenue recognized is adjusted for commissions, volume rebates and discounts at the point in time control is transferred.

Amounts charged to customers for shipping and handling are recognized as revenue, and shipping and handling costs incurred by CPPI are reported as a component of freight and other distribution costs.

Income taxes

Income tax expense comprises current and deferred taxes. Current and deferred taxes are recognized in net income except to the extent that they relate to items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using the tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous periods.

CPPI recognizes deferred income tax in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is measured at tax rates expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred income tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Investment tax credits are credited to manufacturing and product costs in the period in which it becomes reasonably assured that the Company is entitled to them. Unused investment tax credits are recorded as other current or long-term assets in the Company’s balance sheet, depending upon when the benefit is expected to be received.

Foreign currency translation

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

The majority of CPPI's sales are denominated in foreign currencies, principally the US dollar. Transactions in foreign currencies are translated to the functional currency at exchange rates on the dates of transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate on that date. Foreign currency differences arising on translation are recognized in net income.

The assets and liabilities of foreign operations are translated to the Canadian dollar at exchange rates on the reporting date. The income and expenses of foreign operations are translated to the Canadian dollar at exchange rates on the transaction dates. Foreign exchange differences are recognized in other comprehensive income.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. Segment results reported to the chief operating decision-maker include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise interest-bearing liabilities, head office expenses, and income tax assets and liabilities. Segment capital expenditure is the total cost incurred during the period to acquire property, plant and equipment and intangible assets.

4. Changes in significant accounting policies

IFRS 9 – Financial Instruments

Effective January 1, 2018, the Company adopted IFRS 9, *Financial Instruments* which supersedes IAS 39, *Financial Instruments: Recognition and Measurement,* and sets out requirements for the recognition, measurement, impairment and derecognition of financial assets and liabilities, as well as general hedge accounting.

While the existing requirements for the classification and measurement of financial liabilities are largely retained under IFRS 9, financial assets are required to be classified as measured at amortized cost, FVOCI or FVTPL. The table below outlines the original measurement categories under IAS 39 and the new measurement categories under IFRS 9 for each class of the Company's financial instruments at January 1, 2018:

	Original Classification Under IAS 39	New Classification Under IFRS 9
Financial Assets:		
Cash and cash equivalents	Loans and receivables	Amortized cost
Trade and other accounts receivables	Loans and receivables	Amortized cost
Financial Liabilities:		
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Operating loans	Other liabilities	Amortized cost

There have been no changes to the carrying values of our financial instruments at January 1, 2018, or to previously reported figures as a result of the classification changes outlined above. There was no impact of the new hedging requirements, as CPPI had no derivative instruments at the transition date.

IFRS 9 also replaces the incurred loss impairment model under IAS 39 with an ECL model. CPPI has elected to apply the simplified approach in determining ECLs, which requires a probability-weighted estimate of expected lifetime credit losses to be recognized upon initial recognition of financial assets measured at amortized cost and contract assets. Credit losses are measured as the present value of cash shortfalls from all possible default events, discounted at the effective interest rate of the financial asset. Loss allowances for financial assets at amortized cost are deducted from the gross carrying amount of the assets. At January 1, 2018, the identified impairment losses were not significant or material and therefore no changes in loss allowances were recognized.

IFRS 15 – Revenue from Contracts with Customers

Effective January 1, 2018, the Company adopted IFRS 15, *Revenue from Contracts with Customers,* which supersedes IAS 18, *Revenue*, IAS 11, *Construction Contracts* and related interpretations, and establishes a comprehensive framework for determining whether, how much and when revenue is recognized.

In the comparative period, revenue was measured at the fair value of consideration received or receivable, net of applicable sales tax, rebates and discounts and after eliminating sales within the Company. Revenue was previously recognized when the significant risks and rewards of ownership had been transferred to the buyer, recovery of consideration was probable, the associated costs and possible returns of the goods could be reliably estimated, there was no continuing management involvement with the goods, and the amount of revenue could be reliably measured. Under the new standard, however, revenue from the sale of goods is measured based on the consideration specified in a contract with a customer and is recognized when a customer obtains control of the goods or services.

The Company has applied the full retrospective method upon transition to IFRS 15, with no resulting quantitative impact to the consolidated financial statements.

5. Accounting Standards Issued and Not Applied

In January 2016, the IASB issued IFRS 16, *Leases*, which will supersede IAS 17, *Leases*, and related interpretations. The required adoption date for IFRS 16 is January 1, 2019. IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. In addition, the nature of expenses related to those leases will change as IFRS 16 replaces straight-line operating lease expense with an amortization expense for right-of-use assets and interest expense on lease liabilities.

IFRS 16 may be applied retrospectively to each prior period presented (full retrospective approach), or with the cumulative effect of adoption recognized at initial application (modified retrospective approach). The Company has elected to apply the modified retrospective approach upon adoption at January 1, 2019, measuring the right-of-use asset at its carrying amount had the standard been applied at commencement of the lease. The short-term and low-value recognition exemptions available under the standard will be utilized, along with certain practical expedients.

Based on lease data as at December 31, 2018, IFRS 16 is estimated to have the following financial statement impact on the Company's consolidated balance sheet at transition on January 1, 2019, with no material impact to 2019 net income:

(millions of Canadian dollars)		As at January 1, 2019
Right-of-use asset, net of accumulated amortization	Increase in assets	$ 1.4
Lease obligation	Increase in liabilities	1.5
Retained earnings	Decrease in equity	0.1

The full quantification of the new standard will be disclosed in the condensed consolidated interim financial statements for the first quarter of 2019.

6. Inventories

(millions of Canadian dollars)	**As at December 31, 2018**	As at December 31, 2017
Pulp	**$ 83.2**	$ 78.5
Paper	**22.2**	14.9
Wood chips and logs	**48.3**	19.9
Materials and supplies	**53.4**	52.2
	$ 207.1	$ 165.5

There were no inventory write-downs at December 31, 2018 or December 31, 2017. Inventory expensed in 2018 includes manufacturing and product costs and amortization.

7. Property, Plant and Equipment and Intangible Assets

(millions of Canadian dollars)	Land and improvements	Buildings, machinery and equipment	Other property, plant and equipment[2]	Construction in progress	Intangible assets[3]	Total property, plant and equipment and intangible assets
Cost						
Balance at January 1, 2017	$ 5.4	$ 1,578.3	$ 41.7	$ 18.3	$ 8.4	$ 1,652.1
Additions[1]	-	-	-	77.5	4.8	82.3
Disposals	-	(38.7)	(25.4)	-	(1.5)	(65.6)
Transfers	-	28.8	23.3	(52.1)	-	-
Balance at December 31, 2017	$ 5.4	$ 1,568.4	$ 39.6	$ 43.7	$ 11.7	$ 1,668.8
Additions[1]	-	-	0.4	113.3	18.7	132.4
Disposals	-	(32.3)	(22.4)	-	(1.7)	(56.4)
Transfers	-	98.2	41.0	(139.2)	-	-
Balance at December 31, 2018	$ 5.4	$ 1,634.3	$ 58.6	$ 17.8	$ 28.7	$ 1,744.8
Amortization						
Balance at January 1, 2017	$ -	$ (1,101.0)	$ (24.0)	$ -	$ (6.7)	$ (1,131.7)
Amortization for the year	-	(53.4)	(20.9)	-	(0.1)	(74.4)
Disposals	-	37.1	25.4	-	1.5	64.0
Balance at December 31, 2017	$ -	$ (1,117.3)	$ (19.5)	$ -	$ (5.3)	$ (1,142.1)
Amortization for the year	-	(56.8)	(22.3)	-	(0.5)	(79.6)
Disposals	-	31.0	22.4	-	1.7	55.1
Balance at December 31, 2018	$ -	$ (1,143.1)	$ (19.4)	$ -	$ (4.1)	$ (1,166.6)
Carrying Amounts						
At January 1, 2017	$ 5.4	$ 477.3	$ 17.7	$ 18.3	$ 1.7	$ 520.4
At December 31, 2017	$ 5.4	$ 451.1	$ 20.1	$ 43.7	$ 6.4	$ 526.7
At December 31, 2018	**$ 5.4**	**$ 491.2**	**$ 39.2**	**$ 17.8**	**$ 24.6**	**$ 578.2**

[1]Net of capital expenditures financed by government grants.
[2] Other property, plant and equipment is comprised of major overhauls and capitalized landfill retirement costs.
[3]At December 31, 2018, intangible assets included $20.2 million of work in progress assets (December 31, 2017 - $5.7 million) and as such had no related amortization in the period.

8. Accounts Payable and Accrued Liabilities

(millions of Canadian dollars)	**As at December 31, 2018**	As at December 31, 2017
Trade payables and accrued liabilities	**$ 137.1**	$ 102.6
Accrued payroll and related liabilities	**44.9**	39.7
Income tax payable	**-**	19.2
	$ 182.0	$ 161.5

9. Operating Loans

(millions of Canadian dollars)	**As at December 31, 2018**	As at December 31, 2017
Available operating loans:		
Operating loan facility	**$ 110.0**	$ 110.0
Letters of credit	**(11.1)**	(9.2)
Total available operating loan facility	**$ 98.9**	$ 100.8

On April 6, 2018, the maturity date of the Company's principal operating loan facility was extended from January 31, 2020 to April 6, 2022. The terms of the Company's operating loan facility include interest payable at floating rates that vary depending on the ratio of debt to total capitalization, and is based on the lenders' Canadian prime rate, bankers' acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin. The facility has certain financial covenants including a covenant based on maximum debt to total capitalization of the Company.

As at December 31, 2018, the Company is in compliance with all covenants relating to its operating loan facility.

10. Long-Term Debt

On December 29, 2017, the Company repaid the full principal balance of its term loan of $50.0 million. Prior to repayment, the interest rate on the term loan was based on the lenders' Canadian prime rate or bankers' acceptance rate in the year of payment.

11. Employee Future Benefits

The Company, in participation with Canfor, has several funded and unfunded defined benefit pension plans, defined contribution plans, and other non-pension post-retirement benefit plans that provide benefits to substantially all salaried employees and certain hourly employees. The defined benefit pension plans are based on years of service and final average salary. CPPI's other non-pension post-retirement benefit plans are non-contributory and include a range of health care and other benefits.

Total cash payments for employee future benefits for 2018 were $17.0 million (December 31, 2017 - $16.8 million), consisting of cash contributed by CPPI to its funded pension plans, cash payments directly to beneficiaries for its unfunded other non-pension post-retirement benefit plans, and cash contributed to its defined contribution and other plans.

Defined benefit plans

CPPI measures its accrued retirement benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year.

As at December 31, 2018, CPPI has one registered defined benefit pension plan for which an actuarial valuation is performed at least every three years. The largest pension plan underwent an actuarial valuation for funding purposes as of December 31, 2017, which was completed in 2018. The next actuarial valuation for funding purposes is currently scheduled for December 31, 2020, to be completed in 2021. In addition, CPPI has other non-contributory benefit plans that provide certain non-pension post-retirement benefits to its members. The other non-contributory plans also underwent an actuarial valuation as of December 31, 2017, which was completed in 2018.

Information about CPPI's defined benefit plans, in aggregate, is as follows:

Fair market value of plan assets	**2018**		2017	
(millions of Canadian dollars)	**Defined Benefit Pension Plans**	**Other Benefit Plans**	Defined Benefit Pension Plans	Other Benefit Plans
Beginning of year	**$ 130.1**	**$ -**	$ 123.9	$ -
Interest income on plan assets	**4.4**	**-**	4.8	-
Return on plan assets greater (less) than discount rate	**(8.1)**	**-**	1.8	-
Employer contributions	**5.0**	**1.6**	4.3	2.7
Employee contributions	**0.1**	**-**	0.1	-
Benefit payments	**(4.7)**	**(1.6)**	(4.7)	(2.7)
Administration expense	**(0.1)**	**-**	(0.1)	-
End of year	**$ 126.7**	**$ -**	$ 130.1	$ -

Plan assets consist of the following:	**As at December 31, 2018**	As at December 31, 2017
	Percentage of Plan Assets	
Asset category		
Equity securities	**14%**	36%
Debt securities	**26%**	8%
Annuities	**60%**	56%
Cash and cash equivalents	**0%**	0%
	100%	100%

Accrued benefit obligations	**2018**		2017	
(millions of Canadian dollars)	**Defined Benefit Pension Plans**	**Other Benefit Plans**	Defined Benefit Pension Plans	Other Benefit Plans
Beginning of year	**$ 158.8**	**$ 54.9**	$ 148.0	$ 83.6
Current service cost	**2.8**	**1.3**	2.9	2.1
Settlement adjustment	**-**	**-**	-	(0.5)
Interest cost	**5.3**	**1.8**	5.7	3.2
Employee contributions	**0.1**	**-**	0.1	-
Benefit payments	**(4.7)**	**(1.6)**	(4.7)	(2.7)
Actuarial loss (gain)	**(6.6)**	**(7.0)**	6.8	(30.3)
Other	**-**	**(0.2)**	-	(0.5)
End of year	**$ 155.7**	**$ 49.2**	$ 158.8	$ 54.9

Of the defined benefit pension plan obligation of $155.7 million (December 31, 2017 - $158.8 million), $140.2 million (December 31, 2017 - $143.3 million) relates to plans that are wholly or partly funded and $15.5 million (December 31, 2017 - $15.5 million) relates to plans that are wholly unfunded, with letters of credit securing $4.4 million (December 31, 2017 - $2.5 million) of the unfunded liability.

The total obligation for the non-pension post-retirement benefit plans of $49.2 million (December 31, 2017 - $54.9 million) is unfunded.

Annuity contracts

The Company purchased $8.9 million (December 31, 2017 - $37.3 million) of buy-in annuities through its defined benefit pension plans during the year, increasing total annuities purchased to $86.0 million at December 31, 2018 (December 31, 2017 - $77.1 million). Future cash flows from the annuities will match the amount and timing of benefits payable under the plans, substantially mitigating the exposure to future volatility in the related pension obligations. Transaction costs of $0.7 million (December 31, 2017 - $1.6 million) related to the purchase were recognized in other comprehensive income (loss), principally reflecting the difference in the annuity rate compared to the discount rate used to value the obligations on a going concern basis.

Voluntary Retiree Buyout Program

In October 2017, certain non-pension post-retirement benefit plan members of the Company were given an offer to receive lump-sum payment in exchange for settlement of their future non-pension post-retirement benefit obligations under the Voluntary Retiree Buyout Program ("the Program"). Acceptance of the offer constitutes an irrevocable election to terminate future benefit obligations by plan members, and as such, settlement was recorded at the time of election by members. The deadline for elections made under the Program was October 31, 2017, and the resulting payments were made from November 2017 through January 2018. Under the program, $1.3 million of non-pension post-retirement benefit obligations were settled and derecognized in 2017, resulting in a settlement adjustment of $0.5 million, which was included in operating income. For the year ended December 31, 2018, $0.3 million was paid out under the Program (December 31, 2017 - $0.5 million).

Medical Services Plan changes

On November 2, 2017, the Legislative Assembly of British Columbia enacted the *Budget Measures Implementation Act, 2017,* which included a 50% reduction in Medical Services Plan ("MSP") premiums effective January 1, 2018. This change in legislation was recognized in actuarial financial assumptions in 2017, and resulted in a $28.5 million pre-tax reduction of the non-pension post-retirement benefit obligation and a corresponding gain recognized through other comprehensive income (loss).

In addition, in measuring the accrued benefit obligation at December 31, 2017, the MSP growth trend rate actuarial financial assumption was reduced from 4.5% to 2.0% resulting in an additional $9.3 million pre-tax gain recognized through other comprehensive income (loss) in 2017.

Reconciliation of funded status of defined benefit plans to amounts recorded in the financial statements

(millions of Canadian dollars)	**December 31, 2018** Defined Benefit Pension Plans	**December 31, 2018** Other Benefit Plans	December 31, 2017 Defined Benefit Pension Plans	December 31, 2017 Other Benefit Plans
Fair market value of plan assets	**$ 126.7**	**$ -**	$ 130.1	$ -
Accrued benefit obligations	**(155.7)**	**(49.2)**	(158.8)	(54.9)
Funded status of plans – deficit	**$ (29.0)**	**$ (49.2)**	$ (28.7)	$ (54.9)
Other pension plans	**(1.8)**	**-**	(1.6)	-
Total accrued benefit liability, net	**$ (30.8)**	**$ (49.2)**	$ (30.3)	$ (54.9)

Components of pension cost

The following table shows the before tax impact on net income and other comprehensive income of the Company's defined benefit pension and other non-pension post-retirement benefit plans:

(millions of Canadian dollars)	**2018** Defined Benefit Pension Plans	**2018** Other Benefit Plans	2017 Defined Benefit Pension Plans	2017 Other Benefit Plans
Recognized in net income				
Current service cost	**$ 2.8**	**$ 1.3**	$ 2.9	$ 2.1
Settlement adjustment	**-**	**-**	-	(0.5)
Administrative cost	**0.1**	**-**	-	-
Interest cost	**0.9**	**1.8**	0.9	3.2
Other	**-**	**(0.2)**	-	(0.2)
Total expense included in net income	**$ 3.8**	**$ 2.9**	$ 3.8	$ 4.6
Recognized in other comprehensive income				
Actuarial (gain) – experience	**$ (2.2)**	**$ (4.1)**	$ (3.3)	$ (0.1)
Actuarial loss (gain) – financial assumptions	**(4.4)**	**(2.9)**	10.1	(30.2)
Return on plan assets less (greater) than discount rate	**8.1**	**-**	(1.8)	-
Administrative costs greater than expected	**-**	**-**	0.1	-
Total loss (gain) in other comprehensive income	**$ 1.5**	**$ (7.0)**	$ 5.1	$ (30.3)

Significant assumptions

The actuarial assumptions used in measuring CPPI's benefit plan provisions and benefit costs are as follows:

	December 31, 2018 Defined Benefit Pension Plans	**December 31, 2018** Other Benefit Plans	December 31, 2017 Defined Benefit Pension Plans	December 31, 2017 Other Benefit Plans
Discount rate	**3.6%**	**3.6%**	3.4%	3.4%
Rate of compensation increases	**3.0%**	**n/a**	3.0%	n/a
Initial medical cost trend rate	**n/a**	**5.5%**	n/a	6.5%
Ultimate medical cost trend rate	**n/a**	**4.5%**	n/a	4.5%
Year ultimate rate is reached	**n/a**	**2022**	n/a	2022

In addition to the significant assumptions listed in the table above, the average life expectancy of a 65-year-old at December 31, 2018 is between 21.1 years and 24.2 years (December 31, 2017 - 21.0 years and 24.1 years). As at December 31, 2018, the weighted average duration of the defined benefit plan obligation, which reflects the average age of the plan members, is 12.0 years (December 31, 2017 - 12.3 years). The weighted average duration of the other benefit plans is 13.3 years (December 31, 2017 - 14.2 years).

Sensitivity analysis

Assumed discount rates and medical cost trend rates have a significant effect on the accrued retirement benefit obligation and related plan assets. A one percentage point change in these assumptions would have the following effects on the accrued retirement benefit obligation, including the hedging impact of plan annuity assets, for 2018:

(millions of Canadian dollars)		1% Increase		1% Decrease
Defined benefit pension plan liabilities, net of annuity assets				
Discount rate	$	(9.9)	$	12.7
Other benefit plan liabilities				
Discount rate	$	(6.5)	$	8.1
Initial medical cost trend rate	$	4.4	$	(4.0)

When taking into account the impact of hedging, 49% (December 31, 2017 - 45%) of the change to the defined benefit pension plans is fully hedged against changes in discount rates and longevity risk (potential increases in life expectancy of plan members) through buy-in annuities, and a further 20% (December 31, 2017 - 17%) is partially hedged through the plan's investment in debt securities.

As at December 31, 2018, contribution payments of $4.7 million are estimated to be made to the Company's defined benefit pension plans in 2019 based on the last actuarial valuation for funding purposes.

Defined contribution and other plans

The total expense recognized in 2018 for CPPI's defined contribution plans was $2.8 million (December 31, 2017 - $2.5 million).

CPPI contributes to a pulp industry pension plan providing pension benefits. This plan is accounted for as a defined contribution plan. Contributions to this plan, not included in the expense for the defined contribution plan above, amounted to $7.6 million in 2018 (December 31, 2017 - $7.3 million).

12. Asset Retirement Obligations

The following table provides a reconciliation of the asset retirement obligations as at December 31, 2018 and December 31, 2017:

(millions of Canadian dollars)		**2018**		2017
Asset retirement obligations at beginning of year	**$**	**5.5**	$	5.4
Accretion expense		**0.1**		0.1
Changes in estimates		**0.4**		-
Asset retirement obligations at end of year	**$**	**6.0**	$	5.5

CPPI's asset retirement obligations represent estimated undiscounted future payments of $9.3 million to remediate landfills at the operations at the end of their useful lives. The payments are expected to occur at periods ranging from 4 to 33 years and have been discounted at risk-free rates ranging from 1.9% to 2.2% (December 31, 2017 - 1.9% to 2.3%).

CPPI has certain assets that have indeterminable retirement dates and, therefore, there is an indeterminate settlement date for the related asset retirement obligations. As a result, no asset retirement obligations are recorded for these assets. These assets include wastewater and effluent ponds that will have to be drained once the related operating facility is closed and storage sites for which removal of chemicals, fuels and other related materials will be required once the related operating facility is closed. When the retirement dates of these assets become determinable and an estimate can be made, an asset retirement obligation will be recorded.

It is possible that changes in future conditions could require a material change in the recognized amount of the asset retirement obligations. The asset retirement obligations balance is included in other long-term provisions on the balance sheet.

13. Share Capital

Authorized

Unlimited number of common shares, no par value.

Issued and fully paid

	2018		2017	
(millions of Canadian dollars, except number of shares)	**Number of Shares**	**Amount**	Number of Shares	Amount
Common shares at beginning of year	**65,251,259**	**$ 480.9**	66,699,368	$ 491.6
Common shares purchased	**(500)**	**-**	(1,448,109)	(10.7)
Common shares at end of year[4]	**65,250,759**	**$ 480.9**	65,251,259	$ 480.9

[4]Based on trade date.

The holders of common shares are entitled to vote at all meetings of shareholders of the Company and are entitled to receive dividends when declared.

Basic net income per share is calculated by dividing the net income available to common shareholders by the weighted average number of common shares outstanding during the period. The weighted average number of common shares outstanding for 2018 is 65,250,763 (December 31, 2017 - 65,887,110), and reflects common shares purchased under the Company's normal course issuer bid.

Normal course issuer bid

On March 5, 2018, the Company renewed its normal course issuer bid whereby up to 3,262,941 common shares or approximately 5% of its issued and outstanding common shares as of March 1, 2018 could be purchased for cancellation.

In 2018, CPPI purchased 500 common shares at an average price of $13.01, and paid $0.1 million related to the purchase of shares in the fourth quarter of 2017. As at December 31, 2018, based on the trade date, there were 65,250,759 common shares of the Company outstanding and Canfor's ownership interest in CPPI was 54.8% (December 31, 2017 - 54.8%).

In 2017, under a previous normal course issuer bid, the Company purchased 1,448,109 common shares for $17.8 million (an average of $12.29 per common share), of which $10.7 million was charged to share capital and $7.1 million was charged to retained earnings.

As at February 21, 2019 there were 65,250,759 common shares of the Company outstanding.

14. Finance Expense, Net

(millions of Canadian dollars)	**2018**	2017
Interest expense on borrowings	**$ (3.3)**	$ (3.7)
Interest expense on retirement benefit obligations, net	**(2.7)**	(4.1)
Interest income	**1.9**	0.7
Other expense	**(0.1)**	(0.1)
Finance expense, net	**$ (4.2)**	$ (7.2)

15. Income Taxes

The components of income tax expense are as follows:

(millions of Canadian dollars)	**2018**	2017
Current	**$ (69.0)**	$ (39.3)
Deferred	**2.3**	0.5
Income tax expense	**$ (66.7)**	$ (38.8)

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

(millions of Canadian dollars)	**2018**	2017
Income tax expense at statutory rate of 27.0% (2017 – 26.0%)	**$ (67.8)**	$ (36.6)
Add (deduct):		
Entities with different income tax rates and other tax adjustments	**0.2**	0.7
Permanent difference from capital gains and other non-deductible items	**0.9**	(0.1)
Change in substantively enacted tax legislation	**-**	(2.8)
Income tax expense	**$ (66.7)**	$ (38.8)

In 2017, the Provincial Government of British Columbia passed legislation increasing the provincial corporate tax rate from 11% to 12% effective January 1, 2018. Accordingly, a $2.8 million increase to income tax expense was recorded in net income in 2017 to record the impact on deferred taxes, with an additional $0.3 million being recorded in other comprehensive income as an income tax recovery on defined benefit plan actuarial losses.

In addition, a tax expense of $1.5 million in relation to actuarial gains on the defined benefit plans (December 31, 2017 - expense of $6.6 million, before the tax rate adjustment) was recorded in other comprehensive income for the year ended December 31, 2018.

The tax effects of the significant components of temporary differences that give rise to deferred income tax assets and liabilities are as follows:

(millions of Canadian dollars)	**As at December 31, 2018**	As at December 31, 2017
Deferred income tax assets		
Retirement benefit obligations	**$ 21.2**	$ 22.6
Other	**3.6**	1.9
	$ 24.8	$ 24.5
Deferred income tax liabilities		
Depreciable capital assets	**$ (91.5)**	$ (91.9)
Other	**(0.1)**	(0.2)
	(91.6)	(92.1)
Total deferred income taxes, net	**$ (66.8)**	$ (67.6)

16. Net Change in Non-Cash Working Capital

(millions of Canadian dollars)	**2018**	2017
Accounts receivable	**$ (2.4)**	$ (24.4)
Inventories	**(41.6)**	0.6
Prepaid expenses	**(2.9)**	4.8
Accounts payable and accrued liabilities	**21.3**	12.6
Net increase in non-cash working capital	**$ (25.6)**	$ (6.4)

17. Related Party Transactions

CPPI undertakes transactions with various related entities. These transactions are in the normal course of business and are generally on similar terms as those accorded to unrelated third parties, except where noted otherwise.

In 2018, the Company depended on Canfor to provide approximately 66% (December 31, 2017 - 62%) of its fibre supply as well as certain key business and administrative services. As a result of these relationships, the Company considers its operations to be dependent on its ongoing relationship with Canfor. The current pricing under one of the Company's Fibre Supply Agreements with Canfor expired on September 1, 2018. During 2018, the Company and Canfor entered into a new pricing agreement, which includes a market-based chip pricing formula. The new pricing agreement is effective July 1, 2018, for a three-year term, to June 30, 2021.

The Company purchased wood chips, logs and hog fuel from Canfor sawmills in the amount of $252.8 million in 2018 (December 31, 2017 - $175.3 million).

Canfor provides certain business and administrative services to CPPI under a services agreement. The total amount charged for the services provided by Canfor in 2018 was $14.8 million (December 31, 2017 - $12.5 million). These amounts are included in manufacturing and product costs and selling and administration costs.

CPPI provides certain business and administrative services to Canfor under an incidental services agreement. The total amount charged for the services provided to Canfor in 2018 was $4.0 million (December 31, 2017 - $3.8 million). These amounts are included as cost recoveries in manufacturing and product costs and selling and administration costs. At December 31, 2018, an outstanding balance of $31.6 million (December 31, 2017 - $13.1 million) was due to Canfor.

The Jim Pattison Group is Canfor's largest shareholder. In August of 2018, The Jim Pattison Group's ownership interest of Canfor increased above 50%, ending the year at 50.9%. During 2018, CPPI sold paper to subsidiaries owned by The Jim Pattison Group totalling $3.0 million (December 31, 2017 - $3.5 million). CPPI also made purchases from subsidiaries owned by The Jim Pattison Group totalling $0.7 million (December 31, 2017 - $0.3 million). No amounts related to these sales or purchases were outstanding as at December 31, 2018 or December 31, 2017.

During 2018, the Company also made contributions to certain post-employment benefit plans for the benefit of CPPI employees and provided services to its joint venture with Licella Fibre Fuel Pty. Ltd. See Note 11, Employee Future Benefits, and Note 22, Licella Pulp Joint Venture, for further details.

Key management personnel

Key management includes members of the Board of Directors and the senior executive management team. The compensation expense for key management for services is as follows:

(millions of Canadian dollars)		**2018**		2017
Short-term benefits	**$**	**3.1**	$	3.4
Post-employment benefits		**0.1**		0.2
	$	**3.2**	$	3.6

Short-term benefits for members of the Board of Directors include an annual retainer as well as attendance fees.

18. Segment Information

The Company has two reportable segments, pulp and paper, which operate as separate business units and represent separate product lines. The following summary describes the operations of each of the Company's reportable segments:

- *Pulp* – Includes purchase of residual fibre, and production and sale of pulp products, including NBSK pulp and BCTMP as well as energy revenues; and
- *Paper* – Includes production and sale of paper products, including bleached, unbleached and coloured kraft paper.

Information regarding the operations of each reportable segment is included in the following table. The accounting policies of the reportable segments are described in Note 3.

In accordance with the new revenue standard, IFRS 15, described in Note 4, sales from contracts with customers have been disaggregated by segment. Sales between the pulp and paper segments are accounted for at prices that approximate fair value. These include sales of slush pulp from the pulp segment to the paper segment. There was no quantitative financial statement impact as a result of the adoption of IFRS 15.

The Company's interest-bearing liabilities are not considered to be segment liabilities, but rather, are managed centrally by the treasury function. Other liabilities are not split by segment for the purposes of allocating resources and assessing performance.

(millions of Canadian dollars)	Pulp	Paper	Unallocated	Elimination Adjustment	Total
Year ended December 31, 2018					
Sales from contracts with customers	**$ 1,192.9**	**$ 180.9**	**$ 0.5**	**$ -**	**$ 1,374.3**
Sales to other segments	**119.7**	**-**	**-**	**(119.7)**	**-**
Operating income (loss)	**248.9**	**11.0**	**(13.3)**	**-**	**246.6**
Amortization	**75.3**	**4.2**	**0.1**	**-**	**79.6**
Capital expenditures[5]	**113.3**	**3.7**	**3.5**	**-**	**120.5**
Identifiable assets	**841.7**	**66.1**	**24.9**	**-**	**932.7**
Year ended December 31, 2017					
Sales from contracts with customers	$ 1,024.5	$ 173.0	$ 0.4	$ -	$ 1,197.9
Sales to other segments	92.0	-	-	(92.0)	-
Operating income (loss)	140.5	26.0	(11.9)	-	154.6
Amortization	70.4	3.9	0.1	-	74.4
Capital expenditures[5]	81.3	1.8	-	-	83.1
Identifiable assets	751.3	55.2	85.7	-	892.2

[5] Capital expenditures represent cash paid for capital assets during the periods and include capital expenditures that were partially financed by government grants.

Geographic information

CPPI's products are marketed worldwide, with sales made to customers in a number of different countries. The following table presents revenue based on the geographical location of CPPI's customers:

(millions of Canadian dollars)	**2018**	2017
Sales by location of customer		
Canada	**$ 81.0**	$ 78.3
Asia	**840.9**	710.0
United States	**323.7**	288.8
Europe	**60.3**	49.1
Other	**68.4**	71.7
	$ 1,374.3	$ 1,197.9

19. Commitments and Contingencies

At the end of the year, CPPI has contractual commitments for the construction of capital assets for $11.8 million (December 31, 2017 - $12.2 million). These commitments are expected to be settled over the following year.

In addition, CPPI has committed to operating leases for property, plant and equipment with future minimum lease payments under these operating leases as follows:

(millions of Canadian dollars)	**As at December 31, 2018**	As at December 31, 2017
Within one year	**$ 0.7**	$ 0.5
Between one and five years	**0.9**	0.7
More than five years	**0.1**	-
Total	**$ 1.7**	$ 1.2

During the year ended December 31, 2018, $2.6 million (December 31, 2017 - $1.9 million) was recognized as an expense for operating leases.

In the ordinary course of its business activities, the Company may be subject to, or enter into, legal actions and claims with customers, unions, suppliers or others.

In circumstances where the Company is not able to determine the outcome of a legal action and claim, no amount is recognized in the consolidated financial statements, with an amount accrued only when a reliable estimate of the obligation can be made. Although there can be no assurance as to the disposition of a legal action and claim, it is the opinion of the Company's management, based upon the information available at this time, that the expected outcome of a legal action and claim, individually or in aggregate, is unlikely to have a material adverse effect on the operating results and financial condition of the Company as a whole.

Energy Agreements

The Company has entered into energy agreements with a BC energy company (the "Energy Agreements") for three of the Company's mills. These agreements are for the commitment of electrical load displacement and the sale of incremental power from the Company's pulp and paper mills. These Energy Agreements include incentive grants from the BC energy company for capital investments to increase electrical generation capacity, and also call for performance guarantees to ensure minimum required amounts of electricity are generated, with penalty clauses if they are not met. As part of these commitments, the Company has entered into standby letters of credit for these guarantees. The standby letters of credit have variable expiry dates, depending on the capital invested and the length of the Energy Agreement involved. As at December 31, 2018, CPPI has $6.7 million of standby letters of credit (December 31, 2017 - $6.7 million) under these agreements, and has no repayment obligations under the terms of any of these agreements.

20. Financial Risk and Capital Management

Financial risk management

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

CPPI's internal 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 Canfor.

Credit risk:

Credit risk is the risk of financial loss to CPPI if a counterparty to a financial instrument fails to meet its contractual obligations.

Financial instruments that are subject to credit risk include cash and cash equivalents, accounts receivable and contract assets. Cash and cash equivalents includes cash held through major Canadian and international financial institutions as well as temporary investments with an original maturity date, or redemption date, of three months or less. The cash and cash equivalents balance at December 31, 2018 is $6.9 million (December 31, 2017 - $76.7 million).

CPPI utilizes credit insurance to mitigate the risk associated with some of its trade accounts receivables. As at December 31, 2018, approximately 78% (December 31, 2017 - 76%) of the outstanding trade accounts receivables are covered under credit insurance. In addition, CPPI requires letters of credit on certain export trade accounts receivables and regularly discounts these letters of credit without recourse. CPPI recognizes the sale of the letters of credit on the settlement date, and accordingly reduces the related trade accounts receivable balance. CPPI's trade accounts receivable balance at December 31, 2018 is $108.6 million, before a loss allowance of $1.0 million (December 31, 2017 - $101.7 million and $0.2 million, respectively). At December 31, 2018, approximately 98% (December 31, 2017 - 99%) of the trade accounts receivable balance are within CPPI's established credit terms.

Liquidity risk:

Liquidity risk is the risk that CPPI will be unable to meet its financial obligations as they come due. The Company manages liquidity risk through regular cash flow forecasting in conjunction with an adequate committed operating loan facility.

At December 31, 2018, and December 31, 2017, CPPI has no amounts drawn on its operating loan facility. At December 31, 2018 CPPI had accounts payable and accrued liabilities of $182.0 million (December 31, 2017 - $161.5 million), all of which are due within twelve months of the balance sheet date.

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, foreign currency, commodity and energy prices.

(i) Interest rate risk:

CPPI is exposed to interest rate risk through its current financial assets and financial obligations bearing variable interest rates.

CPPI may use interest rate swaps to reduce its exposure to financial obligations bearing variable interest rates.

At December 31, 2018 and December 31, 2017, CPPI had no fixed interest rate swaps outstanding.

(ii) Currency risk:

CPPI is exposed to foreign exchange risk primarily related to the US dollar, as CPPI products are sold globally with prices primarily denominated in US dollars or linked to prices quoted in US dollars with certain expenditures transacted in US dollars. In addition, the Company holds financial assets and liabilities in US dollars. These primarily include US dollar bank accounts, investments and trade accounts.

An increase (decrease) in the value of the Canadian dollar by US$0.01 would result in a pre-tax loss (gain) of approximately $1.2 million in relation to working capital balances denominated in US dollars at year end (including cash, accounts receivable and accounts payable).

A portion of the currency risk associated with US dollar denominated sales is naturally offset by US dollar denominated expenses. A portion of the remaining exposure is sometimes covered by foreign exchange collar contracts that effectively limit the minimum and maximum Canadian dollar recovery related to the sale of those US dollars.

CPPI had no foreign exchange derivatives outstanding at December 31, 2018 and December 31, 2017.

(iii) Commodity price risk:

CPPI's financial performance is dependent on the selling price of its products and the purchase price of raw material inputs. Consequently, CPPI is exposed to changes in commodity prices for pulp and paper, as well as changes in fibre, freight, chemical and energy prices. The markets for pulp and paper are cyclical and are influenced by a variety of factors. These factors include periods of excess supply due to industry capacity additions, periods of decreased demand due to weak global economic activity, inventory destocking by customers and fluctuations in currency exchange rates. During periods of low prices, CPPI is subject to reduced revenues and margins, which adversely impact profitability.

From time to time, CPPI enters into futures contracts on commodity exchanges for pulp. Under the Company's Price Risk Management Controls Policy, up to 1% of pulp sales may be sold in this way.

CPPI had no pulp futures contracts outstanding at December 31, 2018 and December 31, 2017.

(iv) Energy price risk:

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

The annual exposure is, from time to time, hedged up to 100% through the use of floating to fixed swap contracts or option contracts with maturity dates up to a maximum of eighteen months. In the case of diesel, CPPI uses Western Texas Intermediate ("WTI") oil contracts to hedge its exposure.

At December 31, 2018 and December 31, 2017, the Company had no WTI oil collars outstanding.

Capital management

CPPI's objectives when managing capital are to maintain a strong balance sheet and a globally competitive cost structure that ensures adequate liquidity to maintain and develop the business through the commodity price cycle.

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

(millions of Canadian dollars)		**As at December 31, 2018**		As at December 31, 2017
Total debt (including operating loans)	**$**	**-**	$	-
Less: Cash and cash equivalents		**(6.9)**		(76.7)
Net cash	**$**	**(6.9)**	$	(76.7)
Total equity		**596.6**		571.4
	$	**589.7**	$	494.7

The Company manages its capital structure through rigorous planning, budgeting and forecasting processes, and ongoing management of operations, investments and capital expenditures. In 2018, to meet CPPI's operating, growth and return on invested capital objectives, the Company's management of capital comprised share purchases and dividends, investment in the Company's operations, development of energy-related assets, and cost reduction initiatives. Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

21. Financial Instruments

CPPI's cash and cash equivalents, trade and other accounts receivables, loans and advances, operating loans, and accounts payable and accrued liabilities are classified as measured at amortized cost in accordance with IFRS 9, adopted by the Company on January 1, 2018 (Note 4). The carrying amounts of these instruments at December 31, 2018, approximate fair value.

When applicable, derivative instruments are classified as measured at FVTPL. IFRS 13, Fair Value Measurement, requires classification of these items within a hierarchy that prioritizes the inputs to fair value measurement.

The three levels of the fair value hierarchy are:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 – Inputs other than quoted prices that are observable for the asset or liability, directly or indirectly;

Level 3 – Inputs that are not based on observable market data.

At times, the Company uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, energy costs and interest rates. As at December 31, 2018 and December 31, 2017, the Company had no derivative financial instruments outstanding.

22. Licella Pulp Joint Venture

On May 27, 2016, CPPI and Licella Fibre Fuel Pty Ltd. ("Licella") agreed to form a joint venture under the name Licella Pulp Joint Venture to investigate opportunities to integrate Licella's Catalytic Hydrothermal Reactor platform into CPPI's pulp mills to economically convert biomass into next generation biofuels and biochemicals. Licella is a subsidiary of Ignite Energy Resources Ltd. ("IER") an Australian energy technology development company.

Under IFRS 11, *Joint Arrangements*, the joint venture is classified as a joint operation and CPPI will recognize its assets, liabilities and transactions, including its share of those incurred jointly, in its consolidated financial statements. For the year ended December 31, 2018, the Company's share of the joint venture's expenses was $2.1 million (December 31, 2017 - $1.1 million) which have been recognized in manufacturing and product costs. The Company is required to contribute the first $20.0 million of any funding requirements, including cash and non-cash contributions, to the joint venture, of which $3.8 million has been contributed as at December 31, 2018.

In March 2017, the Canadian Federal Government through its Sustainable Development Technology Canada program announced the funding over several years of approximately $13.2 million, contingent on future spending. Advance funding of $1.9 million was received in April 2018 for the period October 1, 2017 through to the time at which the terms of funding have been met, which is currently estimated as March 31, 2019. Of this amount, $0.7 million has been recognized as an offset to costs within manufacturing and product costs for the year ended December 31, 2018.

23. Special Dividend

On November 13, 2018, the Company paid a special dividend of $146.8 million ($2.25 per share) to the shareholders of the Company. The special dividend was paid as a result of strong cash generated by the business over the last year.

24. Subsequent Event

On February 21, 2019, the Board of Directors declared a quarterly dividend of $0.0625 per share, payable on March 13, 2019, to the shareholders of record on March 6, 2019.