2018

CANFOR CORPORATION

QUARTER TWO

Interim Report

FOR THE THREE MONTHS
ENDED JUNE 30, 2018

To Our Shareholders

Canfor Corporation reported second quarter 2018 results:

Highlights

- Record adjusted operating income of $334 million driven by historically high lumber prices and record-high pulp and paper earnings; record-high quarterly sales of $1.46 billion
- Adjusted net income of $214 million, or $1.66 per share
- Net cash of $174 million, or 7.9% net cash to total capitalization, at June 30, 2018

Financial Results

The following table summarizes selected financial information for the Company for the comparative periods:

(millions of Canadian dollars, except per share amounts)	**Q2 2018**	Q1 2018	**YTD 2018**	Q2 2017	YTD 2017
Sales	**$ 1,459.5**	$ 1,233.5	**$ 2,693.0**	$ 1,159.6	$ 2,264.8
Reported operating income before amortization	**$ 349.7**	$ 268.6	**$ 618.3**	$ 193.1	$ 362.2
Reported operating income	**$ 282.1**	$ 203.8	**$ 485.9**	$ 131.0	$ 237.8
Adjusted operating income before amortization[1]	**$ 401.4**	$ 303.5	**$ 704.9**	$ 228.7	$ 397.8
Adjusted operating income[1]	**$ 333.8**	$ 238.7	**$ 572.5**	$ 166.6	$ 273.4
Net income[2]	**$ 169.8**	$ 112.2	**$ 282.0**	$ 81.3	$ 147.4
Net income per share, basic and diluted[2]	**$ 1.32**	$ 0.87	**$ 2.19**	$ 0.61	$ 1.11
Adjusted net income[2]	**$ 214.1**	$ 145.4	**$ 359.5**	$ 104.2	$ 163.5
Adjusted net income per share, basic and diluted[2]	**$ 1.66**	$ 1.13	**$ 2.79**	$ 0.78	$ 1.23

[1] Adjusted for countervailing and anti-dumping duty deposits expensed for accounting purposes (expense of $51.7 million in the second quarter of 2018, expense of $34.9 million in the first quarter of 2018, and expense of $35.6 million in the second quarter of 2017).

[2] Attributable to equity shareholders of the Company.

The Company reported operating income of $282.1 million for the second quarter of 2018, up $78.3 million from reported operating income of $203.8 million for the first quarter of 2018, with the increase reflecting significantly higher lumber segment operating earnings and record-high pulp and paper segment operating earnings. Reported results for the second quarter of 2018 included a net duty expense of $51.7 million, at a current effective countervailing duty ("CVD") and anti-dumping duty ("ADD") rate of 14.94%, compared to $34.9 million in the first quarter of 2018 and $35.6 million in the second quarter of 2017. After adjusting for duties, operating income was $333.8 million for the second quarter of 2018, up $95.1 million from similarly adjusted operating income in the first quarter of 2018.

Adjusted lumber segment earnings largely reflected record Western Spruce/Pine/Fir ("Western SPF") and Southern Yellow Pine ("SYP") benchmark lumber prices, a 2 cent, or 2% weaker Canadian dollar and increased shipment and production volumes following the significant weather-related transportation and operational challenges experienced in the first quarter of 2018. These factors more than outweighed the impact of moderately higher unit log costs in Western Canada as a result of increased market-based stumpage and upward pressure on purchased wood costs, as well as higher duties linked to improved shipments and sales realizations in the current quarter. Pulp and paper segment earnings largely reflected favourable Northern Bleached Softwood Kraft ("NBSK") pulp unit sales realizations, increased shipments following the aforementioned transportation challenges, and to a lesser extent improved NBSK pulp mill productivity, which more than offset the impact of scheduled maintenance outages and market-related fibre cost increases in the quarter.

North American lumber demand was solid across all segments of the market in the second quarter of 2018. US housing starts averaged 1,262,000 units on a seasonally adjusted basis, down 4% from the previous quarter and up 8% from the second quarter of 2017. Single-family starts, which consume a higher proportion of lumber, were up 1% from the previous quarter, while multi-family starts were down 16% compared to the first quarter of 2018. Canadian housing construction activity remained solid in the current quarter, at an average of 219,000 units on a seasonally adjusted basis. Offshore lumber demand from China, Japan and other regions was stable through the second quarter, particularly for the Company's increasing percentage of higher-value lumber products.

The average benchmark North American Random Lengths Western SPF 2x4 #2&Btr price was US$598 per Mfbm, up US$85 per Mfbm, or 17%, compared to the first quarter of 2018, with more modest price increases seen across wider-width dimensions. The average benchmark North American Random Lengths SYP East 2x4 #2 price was

US$589 per Mfbm, up US$23 per Mfbm, or 4%, compared to the first quarter of 2018, with more pronounced price increases in 2x6 and 2x10 #2 dimensions, in part reflecting seasonally higher demand. Solid demand coupled with supply constraints contributed to a sharp increase in benchmark lumber prices in April and May, before prices came off their record-high levels through June as transportation availability slowly improved. Offshore lumber realizations saw more modest increases when compared to North America, due in part to the nature of pricing, much of which is negotiated monthly or quarterly in advance.

Total lumber production, at 1.31 billion board feet, was moderately higher than the prior quarter reflecting productivity gains in Western Canada following the extreme winter weather experienced in the first quarter of 2018, as well as the benefit of recent capital expenditures and fewer statutory holidays in the current quarter. Total lumber shipments, at 1.35 billion board feet, were up 13% from the previous quarter aided by solid demand and the drawdown of finished inventory as transportation networks slowly improved. Unit manufacturing costs in the second quarter of 2018 were slightly higher than the previous quarter as the per unit impact of gains in productivity and the benefit of stable log costs in the US South largely offset market-based stumpage increases and higher purchased wood costs in Western Canada.

Global softwood pulp markets remained strong through the second quarter of 2018, with near-record high US-dollar NBSK pulp list prices to China reflecting tighter supply during the traditional spring maintenance period as well as healthy global demand. Average NBSK pulp unit sales realizations were moderately higher than the previous quarter reflecting the weaker Canadian dollar combined with rising US-dollar NBSK pulp list pricing in other regions, particularly North America. Average Bleached Chemi-Thermo Mechanical Pulp ("BCTMP") unit sales realizations showed a moderate decrease quarter-over-quarter, with lower US-dollar pricing more than offsetting the weaker Canadian dollar.

Pulp shipments were up 6% from the previous quarter, reflecting strong market demand and an unwinding of inventory resulting from the transportation challenges in the previous quarter. Pulp production was down 5% from the previous quarter following scheduled maintenance outages at CPPI's Prince George NBSK pulp mill, as well as at its Taylor BCTMP mill, which reduced NBSK pulp production by approximately 4,000 tonnes and BCTMP production by approximately 17,000 tonnes, offset in part by improved productivity at CPPI's NBSK pulp mills. The scheduled maintenance outage at the Prince George pulp mill was completed ahead of schedule. The Taylor BCTMP mill's reduced production included extended downtime in connection with the commissioning of its previously announced energy project, which is now achieving anticipated operating rates. Pulp unit manufacturing costs were moderately higher than the previous quarter, with seasonally lower energy prices and usage partly offsetting market-driven increases in fibre costs and higher unit costs associated with the aforementioned scheduled outages.

Looking ahead, the US housing market is forecast to continue its ongoing gradual recovery through the balance of 2018. North American lumber prices are projected to remain solid, and high by historical standards, in the third quarter of 2018 reflecting solid seasonal demand, while transportation networks are anticipated to continue their slow return toward normal service levels through the quarter. For the Company's key offshore lumber markets, demand is anticipated to remain solid through the third quarter of 2018, particularly in Japan.

Notwithstanding some seasonal weakness in China during the traditionally slower summer months, global softwood kraft pulp markets are projected to be balanced through the third quarter of 2018. For the months of July and August 2018, CPPI announced NBSK pulp list price increases in North America of US$40 per tonne and US$30 per tonne, respectively. Results in the third quarter of 2018 will include a scheduled maintenance outage at Northwood, CPPI's largest NBSK pulp mill, with a projected 28,000 tonnes of reduced NBSK pulp production, combined with higher associated maintenance costs and lower projected shipment volume. Bleached kraft paper demand is anticipated to remain stable through the third quarter of 2018.

Conrad A. Pinette
Chairman

Don B. Kayne
President and Chief Executive Officer

Canfor Corporation
Second Quarter 2018
Management's Discussion and Analysis

This interim Management's Discussion and Analysis ("MD&A") provides a review of Canfor Corporation's ("Canfor" or "the Company") financial performance for the quarter ended June 30, 2018 relative to the quarters ended March 31, 2018 and June 30, 2017, and the financial position of the Company at June 30, 2018. It should be read in conjunction with Canfor's unaudited interim consolidated financial statements and accompanying notes for the quarters ended June 30, 2018 and 2017, as well as the 2017 annual MD&A and the 2017 audited consolidated financial statements and notes thereto, which are included in Canfor's Annual Report for the year ended December 31, 2017 (available at www.canfor.com). The financial information in this interim MD&A has been prepared in accordance with International Financial Reporting Standards ("IFRS"), which is the required reporting framework for Canadian publicly accountable enterprises.

Throughout this discussion, reference is made to Operating Income before Amortization and Adjusted Operating Income before Amortization which Canfor considers to be a relevant indicator for measuring 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. Reference is also made to Adjusted Shareholder Net Income (calculated as Shareholder Net income less specific items affecting comparability with prior periods – for the full calculation, see the reconciliation included in the section "Analysis of Specific Material Items Affecting Comparability of Net Income") and Adjusted Shareholder Net Income per Share (calculated as Adjusted Shareholder Net Income divided by the weighted average number of shares outstanding during the period). Operating Income before Amortization, Adjusted Shareholder Net Income and Adjusted Shareholder Net Income per Share are not generally accepted earnings measures and should not be considered as an alternative to net income or cash flows as determined in accordance with IFRS. As there is no standardized method of calculating these measures, Canfor's Operating Income before Amortization, Adjusted Shareholder Net Income and Adjusted Shareholder Net Income per Share may not be directly comparable with similarly titled measures used by other companies. Reconciliations of Operating Income before Amortization to Operating Income and Adjusted Shareholder Net Income to Net Income reported in accordance with IFRS are included in this MD&A. Throughout this discussion, reference is made to the current quarter, which refers to the results for the second quarter of 2018.

Factors that could impact future operations are also discussed. These factors may be influenced by both 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; currency exchange rates; interest rates; changes in law and public policy; the outcome of labour and trade disputes; and opportunities available to or pursued by Canfor.

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

All financial references are in millions of Canadian dollars unless otherwise noted. The information in this report is as at July 25, 2018.

Forward Looking Statements

Certain statements in this MD&A constitute "forward-looking statements" which involve known and unknown risks, uncertainties and other factors that may cause actual results to be materially different from any future results, performance or achievements expressed or implied by such statements. Words such as "expects", "anticipates", "projects", "intends", "plans", "will", "believes", "seeks", "estimates", "should", "may", "could", and variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are based on management's current expectations and beliefs and actual events or results may differ materially. There are many factors that could cause such actual events or results expressed or implied by such forward-looking statements to differ materially from any future results expressed or implied by such statements. Forward-looking statements are based on current expectations and the Company assumes no obligation to update such information to reflect later events or developments, except as required by law.

SECOND QUARTER 2018 OVERVIEW

Selected Financial Information and Statistics

(millions of Canadian dollars, except per share amounts)	Q2 2018	Q1 2018	YTD 2018	Q2 2017	YTD 2017
Operating income (loss) by segment:					
Lumber	**$ 203.4**	$ 125.9	**$ 329.3**	$ 110.4	$ 194.1
Pulp and Paper	**$ 85.4**	$ 85.1	**$ 170.5**	$ 31.5	$ 66.7
Unallocated and Other[1]	**$ (6.7)**	$ (7.2)	**$ (13.9)**	$ (10.9)	$ (23.0)
Total operating income	**$ 282.1**	$ 203.8	**$ 485.9**	$ 131.0	$ 237.8
Add: Amortization[2]	**$ 67.6**	$ 64.8	**$ 132.4**	$ 62.1	$ 124.4
Total operating income before amortization	**$ 349.7**	$ 268.6	**$ 618.3**	$ 193.1	$ 362.2
Add (deduct):					
Working capital movements	**$ 61.9**	$ (152.1)	**$ (90.2)**	$ 92.3	$ (12.9)
Defined benefit plan contributions, net	**$ (7.3)**	$ (7.3)	**$ (14.6)**	$ (6.6)	$ (12.6)
Income taxes paid, net	**$ (24.3)**	$ (46.8)	**$ (71.1)**	$ (19.3)	$ (18.1)
Adjustment to accrued duties[3]	**$ (10.1)**	$ (12.9)	**$ (23.0)**	$ -	$ -
Gain on sale of Anthony EACOM Inc.	**$ -**	$ -	**$ -**	$ -	$ (4.0)
Other operating cash flows, net[4]	**$ -**	$ 22.7	**$ 22.7**	$ (5.9)	$ 11.8
Cash from operating activities	**$ 369.9**	$ 72.2	**$ 442.1**	$ 253.6	$ 326.4
Add (deduct):					
Capital additions, net	**$ (87.6)**	$ (56.4)	**$ (144.0)**	$ (61.7)	$ (100.6)
Finance expenses paid	**$ (7.3)**	$ (3.7)	**$ (11.0)**	$ (6.4)	$ (9.6)
Distributions paid to non-controlling interests	**$ (2.0)**	$ (1.8)	**$ (3.8)**	$ (2.2)	$ (6.0)
Repayment of long-term debt	**$ (0.1)**	$ (0.1)	**$ (0.2)**	$ (0.1)	$ (0.1)
Share purchases	**$ -**	$ (4.2)	**$ (4.2)**	$ -	$ -
Proceeds received from sale of Anthony EACOM Inc.	**$ -**	$ -	**$ -**	$ 1.2	$ 6.6
Proceeds received from sale of Lakeland Winton	**$ -**	$ -	**$ -**	$ 15.0	$ 15.0
Acquisitions	**$ -**	$ -	**$ -**	$ (14.4)	$ (56.2)
Proceeds from long-term debt	**$ -**	$ -	**$ -**	$ -	$ 1.7
Foreign exchange gain (loss) on cash and cash equivalents	**$ 1.9**	$ 1.4	**$ 3.3**	$ (2.0)	$ (2.1)
Other, net[4]	**$ 1.9**	$ 0.5	**$ 2.4**	$ (4.3)	$ (0.8)
Change in cash / operating loans	**$ 276.7**	$ 7.9	**$ 284.6**	$ 178.7	$ 174.3
ROIC – Consolidated period-to-date[5]	**9.5%**	6.6%	**16.2%**	4.8%	8.8%
Average exchange rate (US$ per C$1.00)[6]	**$ 0.774**	$ 0.791	**$ 0.782**	$ 0.744	$ 0.750

[1] Higher Unallocated and Other in 2017 largely attributable to higher legal costs related to the expiry of the Softwood Lumber Agreement.
[2] Amortization includes amortization of certain capitalized major maintenance costs.
[3] Adjusted to true-up anti-dumping duty deposits expensed for accounting purposes to current accrual rates.
[4] Further information on cash flows may be found in the Company's unaudited interim consolidated financial statements.
[5] Consolidated Return on Invested Capital ("ROIC") is equal to operating income/loss plus realized gains/losses on derivatives, equity income/loss from joint venture and other income/expense, all net of minority interest, divided by the average invested capital during the period. Invested capital is equal to capital assets, plus long-term investments and net non-cash working capital, all excluding minority interest components.
[6] Source – Bank of Canada (monthly average rate for the period).

Analysis of Specific Material Items Affecting Comparability of Shareholder Net Income

After-tax impact, net of non-controlling interests (millions of Canadian dollars, except per share amounts)		**Q2 2018**		**Q1 2018**		**YTD 2018**		**Q2 2017**		**YTD 2017**
Shareholder net income, as reported	**$**	**169.8**	$	112.2	**$**	**282.0**	$	81.3	$	147.4
Foreign exchange (gain) loss on long-term debt and duties receivable	**$**	**1.0**	$	1.9	**$**	**2.9**	$	(2.9)	$	(3.9)
Countervailing and anti-dumping duty deposit expense, net	**$**	**37.7**	$	25.5	**$**	**63.2**	$	25.8	$	25.8
(Gain) loss on derivative financial instruments	**$**	**5.6**	$	5.8	**$**	**11.4**	$	-	$	(2.4)
Gain on sale of Anthony EACOM Inc.	**$**	**-**	$	-	**$**	**-**	$	-	$	(3.4)
Net impact of above items	**$**	**44.3**	$	33.2	**$**	**77.5**	$	22.9	$	16.1
Adjusted shareholder net income	**$**	**214.1**	$	145.4	**$**	**359.5**	$	104.2	$	163.5
Shareholder net income per share (EPS), as reported	**$**	**1.32**	$	0.87	**$**	**2.19**	$	0.61	$	1.11
Net impact of above items per share	**$**	**0.34**	$	0.26	**$**	**0.60**	$	0.17	$	0.12
Adjusted shareholder net income per share	**$**	**1.66**	$	1.13	**$**	**2.79**	$	0.78	$	1.23

The Company reported operating income of $282.1 million for the second quarter of 2018, up $78.3 million from reported operating income of $203.8 million for the first quarter of 2018, with the increase reflecting significantly higher lumber segment operating earnings and record-high pulp and paper segment operating earnings. Reported results in the second quarter of 2018 include a net duty expense of $51.7 million, at a combined effective countervailing duty ("CVD") and anti-dumping duty ("ADD") rate of 14.94%, compared to $34.9 million in the first quarter of 2018 and $35.6 million in the second quarter of 2017. After adjusting for duties, operating income was $333.8 million for the second quarter of 2018, up $95.1 million from similarly adjusted operating income in the first quarter of 2018.

Adjusted lumber segment earnings largely reflected record Western Spruce/Pine/Fir ("Western SPF") and Southern Yellow Pine ("SYP") benchmark lumber prices, a 2 cent, or 2% weaker Canadian dollar and increased shipment and production volumes following the significant weather-related transportation and operational challenges experienced in the first quarter of 2018. These factors more than outweighed the impact of moderately higher unit log costs in Western Canada as a result of increased market-based stumpage and upward pressure on purchased wood costs, as well as higher duties linked to improved shipments and sales realizations in the current quarter. Pulp and paper segment earnings largely reflected favourable Northern Bleached Softwood Kraft ("NBSK") pulp unit sales realizations, increased shipments following the aforementioned transportation challenges, and to a lesser extent improved NBSK pulp mill productivity, which more than offset the impact of scheduled maintenance outages and market-related fibre cost increases in the quarter.

The current quarter's reported operating income was up $151.1 million from $131.0 million reported for the second quarter of 2017, reflecting a $93.0 million increase in lumber segment earnings and a $53.9 million increase in earnings for the pulp and paper segment. The increase in lumber segment earnings primarily reflected higher Western SPF and SYP lumber unit sales realizations, driven by historically high prices, offset in part by market-driven increases in purchased wood costs and stumpage, increased logging and hauling costs in Western Canada, and a 3 cent, or 4%, stronger Canadian dollar. Pulp and paper segment results reflected substantially higher average NBSK pulp and Bleached Chemi-Thermo Mechanical Pulp ("BCTMP") US-dollar pricing combined with increased shipments and pulp production. These factors significantly outweighed the stronger Canadian dollar and higher market-based fibre costs.

OPERATING RESULTS BY BUSINESS SEGMENT

Lumber

Selected Financial Information and Statistics – Lumber

(millions of Canadian dollars, unless otherwise noted)	Q2 2018	Q1 2018	YTD 2018	Q2 2017	YTD 2017
Sales	**$ 1,063.2**	$ 873.9	**$ 1,937.1**	$ 878.7	$ 1,674.8
Operating income before amortization	**$ 251.3**	$ 171.5	**$ 422.8**	$ 154.0	$ 281.2
Operating income	**$ 203.4**	$ 125.9	**$ 329.3**	$ 110.4	$ 194.1
Countervailing and anti-dumping duty deposits[7]	**$ 51.7**	$ 34.9	**$ 86.6**	$ 35.6	$ 35.6
Adjusted operating income	**$ 255.1**	$ 160.8	**$ 415.9**	$ 146.0	$ 229.7
Average SPF 2x4 #2&Btr lumber price in US$[8]	**$ 598**	$ 513	**$ 556**	$ 388	$ 368
Average SPF price in Cdn$	**$ 773**	$ 649	**$ 711**	$ 521	$ 491
Average SYP 2x4 #2 lumber price in US$[9]	**$ 589**	$ 566	**$ 578**	$ 476	$ 479
U.S. housing starts (thousand units SAAR)[10]	**1,262**	1,317	**1,290**	1,171	1,208
Production – SPF lumber (MMfbm)[11]	**947.7**	888.7	**1,836.4**	951.5	1,887.9
Production – SYP lumber (MMfbm)[11]	**367.2**	351.4	**718.6**	358.8	721.7
Shipments – SPF lumber (MMfbm)[12]	**970.3**	851.2	**1,821.5**	965.0	1,855.5
Shipments – SYP lumber (MMfbm)[12]	**380.4**	344.6	**725.0**	355.5	702.4

[7] Adjusted for countervailing and anti-dumping duty deposits expensed for accounting purposes in the first and second quarters of 2018 and second quarter of 2017 to true-up the preliminary anti-dumping duty deposits expensed for accounting purposes to current accrual rates.
[8] Western Spruce/Pine/Fir, per thousand board feet (Source – Random Lengths Publications, Inc.).
[9] Southern Yellow Pine, Eastside, per thousand board feet (Source – Random Lengths Publications, Inc.).
[10] Source – US Census Bureau, seasonally adjusted annual rate ("SAAR").
[11] Excluding production of trim blocks.
[12] Canfor-produced lumber, including lumber purchased for remanufacture and engineered wood, excluding trim blocks, wholesale shipments and lumber sold on behalf of third parties.

Markets

North American lumber demand was solid across all segments of the market in the second quarter of 2018. US housing starts averaged 1,262,000 units on a seasonally adjusted basis, down 4% from the previous quarter and up 8% from the second quarter of 2017. Single-family starts, which consume a higher proportion of lumber, were up 1% from the previous quarter, while multi-family starts were down 16% compared to the first quarter of 2018. Canadian housing construction activity remained near historical highs in the second quarter of 2018, at an average of 219,000 units on a seasonally adjusted basis, down slightly from the previous quarter. Offshore lumber shipments were up 19% from the previous quarter, reflecting slowly improving transportation networks combined with solid demand in key offshore lumber markets, primarily China and Japan.

Sales

Sales for the lumber segment for the second quarter of 2018 were $1.06 billion, compared to $873.9 million in the previous quarter and $878.7 million for the second quarter of 2017. The 22% increase in sales revenue compared to the prior quarter and 21% increase compared to the second quarter of 2017 principally reflected significantly higher Western SPF and SYP lumber unit sales realizations.

Total lumber shipments in the second quarter of 2018 were 1.35 billion board feet, 13% higher than the previous quarter reflecting both solid demand and the release of inventory as transportation networks slowly returned to more normal service levels following the severe winter weather in the first quarter of 2018. Total lumber shipments were up slightly compared to the second quarter of 2017, in part reflecting increased production available for sale in the US South following recent capital upgrades and, to a lesser extent, the benefit of increased shipments following the transportation constraints experienced in the first quarter of 2018.

Western SPF lumber unit sales realizations were well up compared to the first quarter of 2018 reflecting higher average benchmark lumber prices and the 2% weaker Canadian dollar. The average benchmark North American Random Lengths Western SPF 2x4 #2&Btr price was US$598 per Mfbm, up US$85 per Mfbm, or 17%, compared to the first quarter of 2018, with more modest price increases seen across wider-width dimensions. The average benchmark North American Random Lengths SYP East 2x4 #2 price was US$589 per Mfbm, up US$23 per Mfbm, or 4%, compared to the first quarter of 2018, with more pronounced price increases in 2x6 and 2x10 #2 dimensions, in part reflecting seasonally higher demand. Solid demand coupled with supply constraints contributed to a sharp increase in benchmark lumber prices in April and May, before coming off their record-high levels through June as transportation availability slowly improved. Offshore lumber realizations saw more modest increases when compared to North America, due in part to the nature of pricing, much of which is negotiated monthly or quarterly in advance.

Compared to the second quarter of 2017, lumber unit sales realizations were up significantly as higher US-dollar Western SPF and SYP benchmark lumber prices outweighed the impact of the 4% stronger Canadian dollar and increased duties in the current quarter. The average North American Random Lengths Western SPF 2x4 #2&Btr price was up US$210 per Mfbm, or 54%, while the SYP East 2x4 #2 price was up US$113 per Mfbm, or 24%, with similar price increases for 2x6 dimensions. More modest price increases were seen in wider-width SYP dimensions.

Total residual fibre revenue in the current quarter was moderately higher than the prior quarter and significantly higher than the second quarter of 2017, largely reflecting increased market-based pricing and, to a lesser degree, improved chip quality. Current quarter log sales reflected lower harvesting activity during the spring break-up period in Western Canada.

Operations

Total lumber production, at 1.31 billion board feet, was 6% higher than the prior quarter, for the most part reflecting productivity gains in Western Canada following the extreme weather experienced in the first quarter of 2018, and, in part, the benefit of recent capital expenditures in the US South and fewer statutory holidays in the current quarter. Total lumber production was up slightly from the second quarter in 2017 reflecting increased production in the US South.

Unit manufacturing costs in the second quarter of 2018 were slightly higher than the previous quarter as the per unit impact of gains in productivity and the benefit of stable log costs in the US South mostly offset market-based stumpage increases and higher purchased wood costs in Western Canada. Compared to the second quarter of 2017, unit manufacturing costs were moderately higher, largely reflecting market-driven increases in purchased wood costs and stumpage, as well as increased logging and hauling costs in Western Canada.

Pulp and Paper

Selected Financial Information and Statistics – Pulp and Paper[13]

(millions of Canadian dollars, unless otherwise noted)	**Q2 2018**	Q1 2018	**YTD 2018**	Q2 2017	YTD 2017
Sales	**$ 396.3**	$ 359.6	**$ 755.9**	$ 280.9	$ 590.0
Operating income before amortization[14]	**$ 105.1**	$ 104.3	**$ 209.4**	$ 50.0	$ 104.0
Operating income	**$ 85.4**	$ 85.1	**$ 170.5**	$ 31.5	$ 66.7
Average NBSK pulp price delivered to China – US$[15]	**$ 910**	$ 910	**$ 910**	$ 670	$ 658
Average NBSK pulp price delivered to China – Cdn$[15]	**$ 1,176**	$ 1,150	**$ 1,164**	$ 901	$ 877
Production – pulp (000 mt)	**296.5**	311.7	**608.2**	275.2	592.3
Production – paper (000 mt)	**30.6**	34.3	**64.9**	33.6	68.2
Shipments – pulp (000 mt)	**328.6**	310.0	**638.6**	276.3	613.4
Shipments – paper (000 mt)	**32.6**	32.0	**64.6**	35.5	69.2

[13] Includes 100% of Canfor Pulp Products Inc., which is consolidated in Canfor's operating results. Pulp production and shipment volumes presented are for both NBSK pulp and BCTMP.
[14] Amortization includes amortization of certain capitalized major maintenance costs.
[15] Per tonne, NBSK pulp list price delivered to China (Resource Information Systems, Inc.).

Markets

Global softwood pulp market conditions remained favourable through the second quarter of 2018, with near-record high US-dollar NBSK pulp list prices reflecting both the traditional spring maintenance period and healthy global demand. Softwood pulp inventories at the end of June 2018 were in the balanced range at 28 days of supply, a decrease of three days from March 2018[16], in part reflecting improved transportation networks in Western Canada, combined with industry maintenance downtime in the second quarter. Market conditions are generally considered balanced when inventories are in the 27-30 days of supply range. Global kraft paper markets showed continued strength through the second quarter of 2018, supported by solid demand from North American and Asian markets.

[16] World 20 data is based on twenty producing countries representing 80% of world chemical market pulp capacity and is based on information compiled and prepared by the Pulp and Paper Products Council ("PPPC").

Global shipments of bleached softwood pulp for the first six months of 2018 were in line with the first six months of 2017[17].

Sales

Total pulp shipments for the second quarter of 2018 were 328,600 tonnes, up 18,600 tonnes, or 6%, from the previous quarter and up 52,300 tonnes, or 19%, from the second quarter of 2017. Pulp shipments in the current quarter benefitted from sustained strong market demand through the quarter combined with an unwinding of inventory resulting from the transportation challenges in the previous quarter. Compared to the second quarter of 2017, the 19% increase in pulp shipments reflected an 8% increase in pulp production quarter-over-quarter coupled with solid market demand and the aforementioned unwinding of transportation constraints in the current quarter.

The average China US-dollar NBSK pulp list price of US$910 per tonne, as published by RISI, was in line with the previous quarter. Average NBSK pulp unit sales realizations were moderately higher than the previous quarter reflecting the weaker Canadian dollar combined with rising US-dollar NBSK pulp list pricing in other regions, particularly North America, and to a lesser extent, the timing of shipments in the previous quarter (versus orders). Average BCTMP unit sales realizations showed a moderate decrease quarter-over-quarter, as a surge in demand and pricing towards the end of 2017 was largely realized in the first quarter of 2018. Although BCTMP demand remained steady, lower US-dollar pricing more than offset the weaker Canadian dollar.

Compared to the second quarter of 2017, the average China US-dollar NBSK pulp list price was up US$240 per tonne, or 36%, while US-dollar list prices on shipments to North America showed more modest gains over the same period. These higher global US-dollar prices resulted in substantially higher average NBSK pulp unit sales realizations, net of the 4% stronger Canadian dollar. Average BCTMP unit sales realizations also increased significantly when compared to the second quarter of 2017, primarily reflecting the improvement in BCTMP market demand which more than offset the stronger Canadian dollar in the second quarter of 2018.

Energy revenues were lower than the first quarter of 2018, primarily reflecting seasonally lower power prices combined with a decrease in power generation related to the aforementioned scheduled maintenance outages in the current period. Energy revenues were modestly higher than the second quarter of 2017, driven by less maintenance outages combined with higher power prices in the current quarter.

Paper shipments in the second quarter of 2018 were 32,600 tonnes, in line with the first quarter of 2018 as the benefit of improving transportation networks throughout the quarter was offset by lower production following a scheduled maintenance outage in the current quarter. Paper shipments were down 2,900 tonnes from the second quarter of 2017, largely a result of the scheduled maintenance outage at CPPI's Prince George paper machine in the current quarter.

Paper unit sales realizations in the second quarter of 2018 saw a modest increase compared to the previous quarter, reflecting higher market-driven US-dollar pricing and the weaker Canadian dollar. Compared to the second quarter of 2017, improved paper unit sales realizations, reflecting favourable US-dollar pricing, more than offset the 4% stronger Canadian dollar.

Operations

Pulp production in the second quarter of 2018 was 296,500 tonnes, down 15,200 tonnes, or 5% from the first quarter of 2018. During the second quarter of 2018, CPPI completed its scheduled maintenance outage ahead of target at its Prince George NBSK pulp mill, which reduced NBSK pulp production by approximately 4,000 tonnes. CPPI also completed a scheduled maintenance outage at its Taylor BCTMP mill, including the completion of the previously announced energy project. Extended downtime associated with the commissioning and start-up of the Taylor mill resulted in reduced BCTMP production of approximately 17,000 tonnes. This was offset in part by improved operating rates at CPPI's NBSK pulp mills following the challenging weather conditions in the first quarter of 2018.

Pulp production in the current quarter showed a modest increase compared to the second quarter of 2017 after taking account of scheduled maintenance outages at CPPI's Northwood NBSK pulp mill and Taylor BCTMP mill in the comparative quarter (which reduced pulp production by approximately 40,000 tonnes).

[17] As reported by PPPC statistics.

Pulp unit manufacturing costs saw a moderate increase compared to the previous quarter of 2018 as increased fibre costs, and costs associated with the aforementioned scheduled maintenance outages more than offset seasonally lower energy prices and usage in the current quarter. The higher fibre costs reflected increased market prices for delivered sawmill residual chips (linked to Canadian dollar NBSK pulp sales realizations) combined with a seasonal improvement in chip quality, offset by a lower proportion of higher-cost whole log chips. Compared to the second quarter of 2017, higher pulp unit manufacturing costs were mostly attributable to market-related increases to fibre costs offset in part by improved productivity quarter-over-quarter.

Paper production for the second quarter of 2018 was 30,600 tonnes, down 11% compared to the previous quarter and 9% compared to the second quarter of 2017, principally reflecting the scheduled maintenance outage completed in the current quarter which reduced paper production by approximately 4,000 tonnes. The outage contributed to higher paper unit manufacturing costs compared to both comparative quarters, which also reflected increased slush pulp costs associated with higher average NBSK pulp sales realizations in the current quarter.

Unallocated and Other Items

Selected Financial Information

(millions of Canadian dollars)	**Q2 2018**	Q1 2018	**YTD 2018**	Q2 2017	YTD 2017
Operating loss of Panels operations[18]	**$ (0.3)**	$ (0.6)	**$ (0.9)**	$ (0.5)	$ (1.2)
Corporate costs	**$ (6.4)**	$ (6.6)	**$ (13.0)**	$ (10.4)	$ (21.8)
Finance expense, net	**$ (6.2)**	$ (6.7)	**$ (12.9)**	$ (7.8)	$ (15.8)
Foreign exchange gain (loss) on long-term debt and duties receivable	**$ (1.2)**	$ (2.2)	**$ (3.4)**	$ 3.4	$ 4.5
Gain (loss) on derivative financial instruments	**$ (7.6)**	$ (8.0)	**$ (15.6)**	$ -	$ 3.2
Other income (expense), net	**$ 3.3**	$ 5.3	**$ 8.6**	$ (3.2)	$ (1.0)

[18] The Panels operations include the Company's PolarBoard oriented strand board ("OSB") plant, which is currently indefinitely idled and its Tackama plywood plant, which has been permanently closed.

Corporate costs were $6.4 million for the second quarter of 2018, in line with the previous quarter and down $4.0 million from the second quarter of 2017 largely as a result of lower costs associated with the softwood lumber dispute.

Net finance expense of $6.2 million for the second quarter of 2018 was down slightly from the previous quarter in part reflecting increased interest income resulting from the Company's improved cash balance. Compared to the second quarter of 2017, net finance expense was down moderately reflecting lower interest expense associated with the Company's employee future benefit plans and the early repayment of CPPI's $50.0 million long-term debt towards the end of 2017 combined with the increase in interest income in the current quarter. In the second quarter of 2018, the Company recognized a foreign exchange loss on its US-dollar term debt held by Canadian entities and a gain on US-denominated duties receivable due to the weaker Canadian dollar at the end of the quarter (see further discussion on the term debt financing in the "Liquidity and Financial Requirements" section).

The Company uses a variety of derivative financial instruments at times as partial economic hedges against unfavourable changes in foreign exchange rates, energy costs, lumber prices, and interest rates. In the second quarter of 2018, the Company recorded a net loss of $7.6 million related to its derivatives instruments, largely reflecting realized losses on lumber future contracts as a result of sharp increases in lumber prices.

Other income, net, of $3.3 million in the second quarter of 2018 principally related to favourable foreign exchange movements on US-dollar denominated working capital balances.

Other Comprehensive Income (Loss)

The following table summarizes Canfor's Other Comprehensive Income (Loss) for the comparable periods:

(millions of Canadian dollars)	Q2 2018	Q1 2018	YTD 2018	Q2 2017	YTD 2017
Defined benefit actuarial gains, net of tax	**$ 1.5**	$ 9.6	**$ 11.1**	$ (26.0)	$ (23.6)
Foreign exchange translation differences for foreign operations, net of tax	**$ 12.5**	$ 15.1	**$ 27.6**	$ (13.3)	$ (16.5)
Other comprehensive income (loss), net of tax	**$ 14.0**	$ 24.7	**$ 38.7**	$ (39.3)	$ (40.1)

In the second quarter of 2018, the Company recorded an after-tax gain of $1.5 million in relation to changes in the valuation of the Company's employee future benefit plans, primarily reflecting a return on plan assets greater than the discount rate. This compared to an after-tax gain of $9.6 million recorded in the first quarter of 2018 and an after-tax loss of $26.0 million recorded in the second quarter of 2017, largely reflecting changes in the discount rates used to value the employee future benefit plans and the return generated on plan assets.

In the second quarter of 2017, the Company purchased $90.5 million of annuities through its defined benefit plans to mitigate its exposure to the future volatility fluctuations in the related pension obligations. At the time of purchase of these annuities, transaction costs of $4.6 million were recognized in Other Comprehensive Income principally reflecting the difference in the annuity rate as compared to the discount rate used to value the pension obligations on a going concern basis.

In addition, the Company recorded a gain of $12.5 million in the second quarter of 2018 related to foreign exchange differences for foreign operations, resulting from the weakening of the Canadian dollar relative to the US dollar at the end of the quarter. This compared to a gain of $15.1 million in the previous quarter and a loss of $13.3 million in the second quarter of 2017.

SUMMARY OF FINANCIAL POSITION

The following table summarizes Canfor's cash flow and selected ratios for and as at the end of the following periods:

(millions of Canadian dollars, except for ratios)	Q2 2018	Q1 2018	YTD 2018	Q2 2017	YTD 2017
Increase in cash and cash equivalents[19]	**$ 274.8**	$ 6.5	**$ 281.3**	$ 140.7	$ 148.4
Operating activities	**$ 369.9**	$ 72.2	**$ 442.1**	$ 253.6	$ 326.4
Financing activities	**$ (9.4)**	$ (9.9)	**$ (19.3)**	$ (56.1)	$ (52.2)
Investing activities	**$ (85.7)**	$ (55.8)	**$ (141.5)**	$ (56.8)	$ (125.8)
Ratio of current assets to current liabilities			**2.6:1**		2.4:1
Net debt (cash) to capitalization[20]			**(7.9)%**		6.9%

[19] Increase in cash and cash equivalents shown before foreign exchange translation on cash and cash equivalents.
[20] Net debt (cash) to capitalization is equal to net debt (cash) divided by net capitalization. Net debt (cash) is equal to interest-bearing debt less cash and cash equivalents on hand. Net capitalization is equal to net debt (cash) plus total equity.

The changes in the components of these cash flows are discussed in the following sections:

Operating Activities

Cash generated from operating activities was $369.9 million in the second quarter of 2018, compared to $72.2 million in the previous quarter and $253.6 million in the second quarter of 2017. The increase in operating cash flows from the previous quarter largely reflected favourable non-cash working capital balances resulting from a seasonal drawdown of log inventories during the spring break-up period in Western Canada, as well as a reduction in lumber and pulp inventories during the quarter as rail service levels improved. Operating cash flows in the second quarter of 2018 also reflected higher cash earnings and, to a lesser extent, lower income taxes paid. Compared to the second quarter of 2017, the increase in operating cash flows was primarily attributable to higher cash earnings, offset in part by higher non-cash working capital balances and increased income taxes paid in the current quarter.

Financing Activities

Cash used in financing activities was $9.4 million in the current quarter, which was broadly in line with the previous quarter. Compared to the second quarter of 2017, cash used in financing activities was down $46.7 million, primarily reflecting the clearing of the drawn balance on the Company's Canadian operating loan facility in second quarter of 2017. During the current quarter, the Company made cash distributions of $2.0 million to non-controlling shareholders, broadly in line with both comparative quarters. The Company had no balance outstanding on its operating loan facility at the end of the second quarter of 2018, similar to the prior quarter and the second quarter of 2017.

Investing Activities

Cash used for investing activities was $85.7 million for the current quarter, compared to $55.8 million for the previous quarter and $56.8 million for the same quarter of 2017. Capital additions were $87.6 million, up $31.2 million from the previous quarter and up $25.9 million from the second quarter of 2017. Current quarter capital expenditures included costs related to upgrades at the Company's sawmills in the US South, as well as various smaller high-returning capital projects aimed at increasing drying capacity and productivity in Western Canada. In the pulp and paper segment, capital expenditures primarily related to the previously announced energy project at CPPI's Northwood and Taylor pulp mills as well as a new ERP software system project, combined with maintenance-of-business capital associated with the aforementioned major scheduled maintenance outages during the quarter.

Liquidity and Financial Requirements

At June 30, 2018, the Company on a consolidated basis had cash of $572.8 million, no amounts drawn on its operating loans, and $66.9 million reserved for several standby letters of credit. At period end, the Company had total available undrawn operating loans of $453.1 million.

At June 30, 2018, excluding CPPI, the Company had undrawn $350.0 million bank operating loan facilities, and $56.1 million reserved for several standby letters of credit, the majority of which related to unregistered pension plans. Interest is payable on the operating loans at floating rates based on the lenders' Canadian prime rate, bankers acceptances, US-dollar base rate or US-dollar LIBOR rate, plus a margin that varies with the Company's debt to total capitalization ratio.

At June 30, 2018, CPPI had an undrawn $110.0 million bank operating loan facility and $10.8 million in letters of credit outstanding under the operating loan facility. On April 6, 2018, the maturity date of CPPI's principal operating loan facility was extended from January 31, 2020 to April 6, 2022.

The Company and CPPI remained in compliance with the covenants relating to their operating loans and long-term debt during the quarter, and expect to remain so for the foreseeable future.

The Company's consolidated net debt (cash) to total capitalization at the end the second quarter of 2018 was (7.9)%. For Canfor, excluding CPPI, net debt to capitalization at the end of the second quarter of 2018 was 0.7%.

On March 5, 2018, the Company renewed its normal course issuer bid whereby it can purchase for cancellation up to 6,439,764 common shares or approximately 5% of its issued and outstanding common shares as of March 1, 2018. The renewed normal course issuer bid is set to expire on March 6, 2019. Canfor did not purchase any common shares in the second quarter of 2018. In the first quarter of 2018, Canfor purchased 19,500 common shares for $0.5 million (average price of $25.64 per common share), and paid an additional $3.7 million related to shares purchased late in the 2017 year. Canfor and CPPI may purchase more shares through the balance of 2018 subject to the terms of their normal course issuer bids.

As at June 30, 2018 and July 25, 2018, Canfor's ownership interest in CPPI remained unchanged from the end of the prior quarter at 54.8%.

OUTLOOK

Lumber

Looking ahead, the US housing market is forecast to continue its ongoing gradual recovery through the balance of 2018. North American lumber prices are projected to remain solid, and high by historical standards, in the third quarter of 2018 reflecting solid seasonal demand, while transportation networks are anticipated to continue their slow return toward normal service levels through the quarter.

For the Company's key offshore lumber markets, demand is anticipated to remain solid through the third quarter of 2018, particularly in Japan.

Pulp and Paper

Notwithstanding some seasonal weakness in China during the traditionally slower summer months, global softwood kraft pulp markets are projected to be balanced through the third quarter of 2018. For the months of July and August 2018, CPPI announced NBSK pulp list price increases in North America of US$40 per tonne and US$30 per tonne, respectively. Results in the third quarter of 2018 will reflect a scheduled maintenance outage at Northwood, CPPI's largest NBSK pulp mill, with a projected 28,000 tonnes of reduced NBSK pulp production, combined with higher associated maintenance costs and lower projected shipment volume.

Bleached kraft paper demand is anticipated to remain stable through the third quarter of 2018.

OUTSTANDING SHARES

At July 25, 2018, there were 128,625,480 common shares of the Company outstanding.

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with International Financial Reporting Standards 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, asset retirement and deferred reforestation obligations, and the determination of ADD expensed and recorded as recoverable 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, other than the possibility of material effects to the income statement from the Company's estimated ADD duty receivable as discussed in Note 14 in the interim financial statements.

ADOPTION OF NEW ACCOUNTING STANDARDS

Effective January 1, 2018, the Company has adopted IFRS 15 *Revenue from Contracts with Customers*. IFRS 15 supersedes IAS 18 *Revenue,* IAS 11 *Construction Contracts* and related interpretations. The standard establishes a framework based on transfer of control for determining how much and when revenue is recognized, and includes expanded disclosure requirements. The adoption of IFRS 15 has had no significant impact on the Company's interim financial statements.

Effective January 1, 2018, the Company has adopted IFRS 9 *Financial Instruments*. IFRS 9 supersedes IAS 39 *Financial Instruments: Recognition and Measurement.* The standard includes requirements for recognition, measurement, impairment and derecognition of financial assets and liabilities, as well as general hedge accounting. The adoption of IFRS 9 has had no significant impact on the Company's interim financial statements.

ACCOUNTING STANDARDS ISSUED AND NOT APPLIED

In January 2016, the International Accounting Standards Board 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 a depreciation expense for right-of-use assets and interest expense on lease liabilities.

It is expected that IFRS 16 will have an impact on the Company's financial statements with recognition of new assets and liabilities for its operating leases. The Company is still in the process of assessing the quantitative impact on its financial statements of this new standard. The Company's future minimum lease payments, on an undiscounted basis, under non-cancellable operating leases at December 31, 2017 were $42.5 million.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

During the quarter ended June 30, 2018, 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 2017 annual statutory reports which are available on www.canfor.com or www.sedar.com.

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, as well as forest fires, can cause logging curtailments, which can affect the supply of raw materials to sawmills 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 products, is generally stronger in the spring and fall months. Shipment volumes are affected by these factors as well as by global supply and demand conditions. Net income is also impacted by fluctuations in Canadian dollar exchange rates, the revaluation to the period end rate of US-dollar denominated working capital balances, US-dollar denominated debt and revaluation of outstanding derivative financial instruments.

SELECTED QUARTERLY FINANCIAL INFORMATION

	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016
Sales and income (millions of Canadian dollars)								
Sales	**$ 1,459.5**	$ 1,233.5	$ 1,182.2	$ 1,165.2	$ 1,159.6	$ 1,105.2	$ 1,043.5	$ 1,101.2
Operating income	**$ 282.1**	$ 203.8	$ 214.2	$ 105.4	$ 131.0	$ 106.8	$ 74.0	$ 97.4
Net income	**$ 198.6**	$ 141.5	$ 152.6	$ 72.6	$ 90.9	$ 77.5	$ 44.2	$ 66.4
Shareholder net income	**$ 169.8**	$ 112.2	$ 131.8	$ 66.2	$ 81.3	$ 66.1	$ 38.0	$ 50.9
Per common share (Canadian dollars)								
Shareholder net income – basic and diluted	**$ 1.32**	$ 0.87	$ 1.02	$ 0.51	$ 0.61	$ 0.50	$ 0.29	$ 0.38
Book value[21]	**$ 15.95**	$ 14.52	$ 13.46	$ 12.32	$ 12.14	$ 11.81	$ 11.17	$ 10.70
Common Share Repurchases								
Share volume repurchased (000 shares)	**-**	20	633	3,526	-	-	-	-
Shares repurchased (millions of Canadian dollars)	**$ -**	$ 0.5	$ 15.7	$ 75.0	$ -	$ -	$ -	$ -
Statistics								
Lumber shipments (MMfbm) [22]	**1,351**	1,196	1,205	1,334	1,333	1,237	1,278	1,343
Pulp shipments (000 mt)	**329**	310	300	303	276	337	275	320
Average exchange rate – US$/Cdn$	**$ 0.774**	$ 0.791	$ 0.786	$ 0.798	$ 0.744	$ 0.756	$ 0.750	$ 0.766
Average Western SPF 2x4 #2&Btr lumber price (US$)	**$ 598**	$ 513	$ 462	$ 406	$ 388	$ 348	$ 315	$ 322
Average SYP (East) 2x4 #2 lumber price (US$)	**$ 589**	$ 566	$ 455	$ 408	$ 476	$ 482	$ 445	$ 414
Average NBSK pulp list price delivered to China (US$)	**$ 910**	$ 910	$ 863	$ 670	$ 670	$ 645	$ 595	$ 595

[21] Book value per common share is equal to shareholders' equity at the end of the period, divided by the number of common shares outstanding at the end of the period.

[22] Canfor-produced lumber, including lumber purchased for remanufacture and engineered wood, excluding trim blocks, wholesale shipments and lumber sold on behalf of third parties.

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

After-tax impact, net of non-controlling interests (millions of Canadian dollars, except for per share amounts)	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016
Shareholder net income, as reported	**$ 169.8**	$ 112.2	$ 131.8	$ 66.2	$ 81.3	$ 66.1	$ 38.0	$ 50.9
Foreign exchange (gain) loss on long-term debt and duties receivable	**$ 1.0**	$ 1.9	$ 0.6	$ (4.4)	$ (2.9)	$ (1.0)	$ 2.7	$ 0.9
Countervailing and anti-dumping duty deposit expense (recovery), net[23]	**$ 37.7**	$ 25.5	$ (17.3)	$ 23.8	$ 26.3	$ -	$ -	$ -
(Gain) loss on derivative financial instruments	**$ 5.6**	$ 5.8	$ 4.8	$ 1.4	$ -	$ (2.4)	$ (1.5)	$ (0.1)
Change in substantively enacted tax rates[24]	**$ -**	$ -	$ (5.1)	$ -	$ -	$ -	$ -	$ -
Mill closure provisions[25]	**$ -**	$ -	$ -	$ (2.4)	$ -	$ -	$ (1.5)	$ -
Gain on sale of Anthony EACOM Inc.[26]	**$ -**	$ -	$ -	$ -	$ -	$ (3.4)	$ -	$ -
Net impact of above items	**$ 44.3**	$ 33.2	$ (17.0)	$ 18.4	$ 23.4	$ (6.8)	$ (0.3)	$ 0.8
Adjusted shareholder net income	**$ 214.1**	$ 145.4	$ 114.8	$ 84.6	$ 104.7	$ 59.3	$ 37.7	$ 51.7
Shareholder net income per share (EPS), as reported	**$ 1.32**	$ 0.87	$ 1.02	$ 0.51	$ 0.61	$ 0.50	$ 0.29	$ 0.38
Net impact of above items per share[27]	**$ 0.34**	$ 0.26	$ (0.13)	$ 0.14	$ 0.18	$ (0.05)	$ -	$ 0.01
Adjusted net income per share[27]	**$ 1.66**	$ 1.13	$ 0.89	$ 0.65	$ 0.78	$ 0.45	$ 0.29	$ 0.39

[23] Adjusted for countervailing and anti-dumping duty deposits expensed for accounting purposes. Results in the fourth quarter of 2017 included an accrued recovery to true-up the preliminary duties to current countervailing and anti-dumping duty rates.
[24] During the fourth quarter of 2017, the Company recorded a $5.1 million decrease, net of minority interest, in deferred tax balances as a result of legislative changes in both Canada and the US.
[25] During the third quarter of 2015, the Company recorded one-time costs of $19.4 million (before-tax) associated with the announced closure of the Canal Flats sawmill. In the third quarter of 2017, $3.2 million (before-tax) of the closure provision was reversed, and in the fourth quarter of 2016, $2.0 million (before-tax) of the closure provision was reversed as a result of lower estimated costs.
[26] On March 31, 2017, Canfor sold its 50% interest in Anthony EACOM Inc. for net proceeds of $21.1 million and recognized a $3.7 million net gain (before-tax).
[27] The year-to-date net impact of the adjusting items per share and adjusted net income per share may not equal the sum of the quarterly per share amounts due to rounding.

Canfor Corporation
Condensed Consolidated Balance Sheets

(millions of Canadian dollars, unaudited)		**As at June 30, 2018**		As at December 31, 2017
ASSETS				
Current assets				
Cash and cash equivalents	**$**	**572.8**	$	288.2
Accounts receivable - Trade		**300.2**		193.0
- Other		**39.9**		42.7
Inventories (Note 3)		**637.6**		628.9
Prepaid expenses and other		**83.2**		54.2
Total current assets		**1,633.7**		1,207.0
Property, plant and equipment		**1,475.3**		1,438.1
Timber licenses		**511.9**		518.3
Goodwill and other intangible assets		**249.3**		228.1
Long-term investments and other (Note 4)		**105.0**		83.3
Retirement benefit surplus (Note 6)		**11.6**		7.9
Deferred income taxes, net		**6.9**		5.6
Total assets	**$**	**3,993.7**	$	3,488.3
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities	**$**	**573.6**	$	470.0
Current portion of deferred reforestation obligations		**49.5**		49.5
Current portion of long-term debt (Note 5(b))		**0.3**		0.3
Total current liabilities		**623.4**		519.8
Long-term debt (Note 5(b))		**398.3**		385.4
Retirement benefit obligations (Note 6)		**256.3**		272.0
Deferred reforestation obligations		**77.4**		63.0
Other long-term provisions		**23.9**		23.7
Deferred income taxes, net		**235.1**		223.4
Total liabilities	**$**	**1,614.4**	$	1,487.3
EQUITY				
Share capital	**$**	**1,014.7**	$	1,014.9
Contributed surplus		**31.9**		31.9
Retained earnings		**922.5**		629.5
Accumulated other comprehensive income		**82.7**		55.1
Total equity attributable to equity shareholders of the Company		**2,051.8**		1,731.4
Non-controlling interests		**327.5**		269.6
Total equity	**$**	**2,379.3**	$	2,001.0
Total liabilities and equity	**$**	**3,993.7**	$	3,488.3

Subsequent Event (Note 8)

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

APPROVED BY THE BOARD

Director, R.S. Smith

Director, C.A. Pinette

Canfor Corporation
Condensed Consolidated Statements of Income

(millions of Canadian dollars, except per share data, unaudited)	3 months ended June 30, **2018**	3 months ended June 30, 2017	6 months ended June 30, **2018**	6 months ended June 30, 2017
Sales	**$ 1,459.5**	$ 1,159.6	**$ 2,693.0**	$ 2,264.8
Costs and expenses				
Manufacturing and product costs	**855.0**	735.5	**1,606.0**	1,484.9
Freight and other distribution costs	**176.5**	164.9	**328.9**	322.3
Countervailing and anti-dumping duty expense, net (Note 14)	**51.7**	35.6	**86.6**	35.6
Amortization	**67.6**	62.1	**132.4**	124.4
Selling and administration costs	**26.2**	30.3	**52.3**	58.6
Restructuring, mill closure and severance costs, net of recovery	**0.4**	0.2	**0.9**	1.8
	$ 1,177.4	$ 1,028.6	**$ 2,207.1**	$ 2,027.6
Equity income	**-**	-	**-**	0.6
Operating income	**282.1**	131.0	**485.9**	237.8
Finance expense, net	**(6.2)**	(7.8)	**(12.9)**	(15.8)
Foreign exchange gain (loss) on long-term debt	**(2.7)**	3.4	**(6.2)**	4.5
Foreign exchange gain on duties receivable (Note 4)	**1.5**	-	**2.8**	-
Gain (loss) on derivative financial instruments (Note 7)	**(7.6)**	-	**(15.6)**	3.2
Other income (expense), net	**3.3**	(3.2)	**8.6**	(1.0)
Net income before income taxes	**270.4**	123.4	**462.6**	228.7
Income tax expense (Note 8)	**(71.8)**	(32.5)	**(122.5)**	(60.3)
Net income	**$ 198.6**	$ 90.9	**$ 340.1**	$ 168.4
Net income attributable to:				
Equity shareholders of the Company	**$ 169.8**	$ 81.3	**$ 282.0**	$ 147.4
Non-controlling interests	**28.8**	9.6	**58.1**	21.0
Net income	**$ 198.6**	$ 90.9	**$ 340.1**	$ 168.4
Net income per common share: (in Canadian dollars)				
Attributable to equity shareholders of the Company				
- Basic and diluted (Note 9)	**$ 1.32**	$ 0.61	**$ 2.19**	$ 1.11

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

Canfor Corporation
Condensed Consolidated Statements of Other Comprehensive Income (Loss)

(millions of Canadian dollars, unaudited)	3 months ended June 30, **2018**	3 months ended June 30, 2017	6 months ended June 30, **2018**	6 months ended June 30, 2017
Net income	**$ 198.6**	$ 90.9	**$ 340.1**	$ 168.4
Other comprehensive income (loss)				
Items that will not be recycled through net income:				
Defined benefit plan actuarial gains (losses) (Note 6)	**2.0**	(35.2)	**15.2**	(31.9)
Income tax recovery (expense) on defined benefit plan actuarial losses/gains (Note 8)	**(0.5)**	9.2	**(4.1)**	8.3
	1.5	(26.0)	**11.1**	(23.6)
Items that may be recycled through net income:				
Foreign exchange translation of foreign operations, net of tax	**12.5**	(13.3)	**27.6**	(16.5)
Other comprehensive income (loss), net of tax	**14.0**	(39.3)	**38.7**	(40.1)
Total comprehensive income	**$ 212.6**	$ 51.6	**$ 378.8**	$ 128.3
Total comprehensive income attributable to:				
Equity shareholders of the Company	**$ 183.8**	$ 45.6	**$ 319.6**	$ 110.9
Non-controlling interests	**28.8**	6.0	**59.2**	17.4
Total comprehensive income	**$ 212.6**	$ 51.6	**$ 378.8**	$ 128.3

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

Canfor Corporation
Condensed Consolidated Statements of Changes in Equity

(millions of Canadian dollars, unaudited)	3 months ended June 30, **2018**	3 months ended June 30, 2017	6 months ended June 30, **2018**	6 months ended June 30, 2017
Share capital				
Balance at beginning of period	**$ 1,014.7**	$ 1,047.7	**$ 1,014.9**	$ 1,047.7
Share purchases (Note 9)	**-**	-	**(0.2)**	-
Balance at end of period	**$ 1,014.7**	$ 1,047.7	**$ 1,014.7**	$ 1,047.7
Contributed surplus				
Balance at beginning of period	**$ 31.9**	$ 31.9	**$ 31.9**	$ (4.6)
Forward purchase liability related to acquisition (Note 12(a))	**-**	-	**-**	36.5
Balance at end of period	**$ 31.9**	$ 31.9	**$ 31.9**	$ 31.9
Retained earnings				
Balance at beginning of period	**$ 751.2**	$ 403.0	**$ 629.5**	$ 351.7
Net income attributable to equity shareholders of the Company	**169.8**	81.3	**282.0**	147.4
Defined benefit plan actuarial gains (losses), net of tax	**1.5**	(22.4)	**10.0**	(20.0)
Share purchases (Note 9)	**-**	-	**(0.3)**	-
Elimination of non-controlling interests (Note 12(a))	**-**	-	**-**	(16.6)
Acquisition of non-controlling interests (Note 9)	**-**	(1.5)	**-**	(2.1)
Non-controlling interests arising from change in partnership interest in pellet plants (Note 13)	**-**	-	**1.3**	-
Balance at end of period	**$ 922.5**	$ 460.4	**$ 922.5**	$ 460.4
Accumulated other comprehensive income				
Balance at beginning of period	**$ 70.2**	$ 85.7	**$ 55.1**	$ 88.9
Foreign exchange translation of foreign operations, net of tax	**12.5**	(13.3)	**27.6**	(16.5)
Balance at end of period	**$ 82.7**	$ 72.4	**$ 82.7**	$ 72.4
Total equity attributable to equity shareholders of the Company	**$ 2,051.8**	$ 1,612.4	**$ 2,051.8**	$ 1,612.4
Non-controlling interests				
Balance at beginning of period	**$ 300.7**	$ 241.7	**$ 269.6**	$ 254.8
Net income attributable to non-controlling interests	**28.8**	9.6	**58.1**	21.0
Defined benefit plan actuarial gains (losses) attributable to non-controlling interests, net of tax	**-**	(3.6)	**1.1**	(3.6)
Distributions to non-controlling interests	**(2.0)**	(2.2)	**(3.8)**	(4.4)
Acquisition of non-controlling interests (Note 9)	**-**	(6.0)	**-**	(8.4)
Elimination of non-controlling interests (Note 12(a))	**-**	-	**-**	(19.9)
Non-controlling interests arising from change in partnership interest in pellet plants (Note 13)	**-**	-	**2.5**	-
Balance at end of period	**$ 327.5**	$ 239.5	**$ 327.5**	$ 239.5
Total equity	**$ 2,379.3**	$ 1,851.9	**$ 2,379.3**	$ 1,851.9

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

Canfor Corporation
Condensed Consolidated Statements of Cash Flows

(millions of Canadian dollars, unaudited)	3 months ended June 30, 2018	3 months ended June 30, 2017	6 months ended June 30, 2018	6 months ended June 30, 2017
Cash generated from (used in):				
Operating activities				
Net income	**$ 198.6**	$ 90.9	**$ 340.1**	$ 168.4
Items not affecting cash:				
Amortization	**67.6**	62.1	**132.4**	124.4
Income tax expense	**71.8**	32.5	**122.5**	60.3
Long-term portion of deferred reforestation obligations	**(3.1)**	(7.5)	**13.8**	8.6
Foreign exchange (gain) loss on long-term debt	**2.7**	(3.4)	**6.2**	(4.5)
Foreign exchange gain on duties receivable (Note 4)	**(1.5)**	-	**(2.8)**	-
Adjustment to accrued duties (Note 14)	**(10.1)**	-	**(23.0)**	-
Changes in mark-to-market value of derivative financial instruments	**2.0**	-	**4.9**	-
Employee future benefits expense	**3.1**	3.3	**6.1**	6.5
Finance expense, net	**6.2**	7.8	**12.9**	15.8
Gain on sale of Anthony EACOM Inc., net	**-**	-	**-**	(4.0)
Equity income	**-**	-	**-**	(0.6)
Other, net	**2.3**	1.5	**4.9**	(4.9)
Defined benefit plan contributions, net	**(7.3)**	(6.6)	**(14.6)**	(12.6)
Income taxes paid, net	**(24.3)**	(19.3)	**(71.1)**	(18.1)
	308.0	161.3	**532.3**	339.3
Net change in non-cash working capital (Note 10)	**61.9**	92.3	**(90.2)**	(12.9)
	369.9	253.6	**442.1**	326.4
Financing activities				
Change in operating bank loans (Note 5(a))	**-**	(40.0)	**-**	(28.0)
Proceeds from long-term debt	**-**	-	**-**	1.7
Repayment of long-term debt	**(0.1)**	(0.1)	**(0.2)**	(0.1)
Finance expenses paid	**(7.3)**	(6.4)	**(11.0)**	(9.6)
Share purchases (Note 9)	**-**	-	**(4.2)**	-
Acquisition of non-controlling interests (Note 9)	**-**	(7.4)	**(0.1)**	(10.2)
Cash distributions paid to non-controlling interests	**(2.0)**	(2.2)	**(3.8)**	(6.0)
	(9.4)	(56.1)	**(19.3)**	(52.2)
Investing activities				
Additions to property, plant and equipment, timber, and intangible assets, net	**(87.6)**	(61.7)	**(144.0)**	(100.6)
Proceeds on disposal of property, plant, and equipment	**0.3**	1.9	**1.1**	8.3
Proceeds on sale of Anthony EACOM Inc., net	**-**	1.2	**-**	6.6
Proceeds on sale of Lakeland Winton	**-**	15.0	**-**	15.0
Acquisition of Beadles & Balfour (Note 12(a))	**-**	-	**-**	(41.8)
Acquisition of Wynndel (Note 12(b))	**-**	(14.4)	**-**	(14.4)
Other, net	**1.6**	1.2	**1.4**	1.1
	(85.7)	(56.8)	**(141.5)**	(125.8)
Foreign exchange gain (loss) on cash and cash equivalents	**1.9**	(2.0)	**3.3**	(2.1)
Increase in cash and cash equivalents*	**276.7**	138.7	**284.6**	146.3
Cash and cash equivalents at beginning of period*	**296.1**	164.2	**288.2**	156.6
Cash and cash equivalents at end of period*	**$ 572.8**	$ 302.9	**$ 572.8**	$ 302.9

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

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

1. Basis of Preparation

These condensed consolidated interim financial statements (the "financial statements") have been prepared in accordance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting*, and include the accounts of Canfor Corporation and its subsidiary entities, including Canfor Pulp Products Inc. ("CPPI"), hereinafter referred to as "Canfor" or "the Company."

These financial statements do not include all of the disclosures required by International Financial Reporting Standards ("IFRS") for annual financial statements. Additional disclosures relevant to the understanding of these financial statements, including the accounting policies applied, can be found in the Company's Annual Report for the year ended December 31, 2017, available at www.canfor.com or www.sedar.com.

Effective January 1, 2018, the Company has adopted IFRS 15 *Revenue from Contracts with Customers*. IFRS 15 supersedes IAS 18 *Revenue,* IAS 11 *Construction Contracts* and related interpretations. The standard establishes a framework based on transfer of control for determining how much and when revenue is recognized, and includes expanded disclosure requirements. The adoption of IFRS 15 has had no significant impact on the Company's interim financial statements.

Effective January 1, 2018, the Company has adopted IFRS 9 *Financial Instruments*. IFRS 9 supersedes IAS 39 *Financial Instruments: Recognition and Measurement.* The standard includes requirements for recognition, measurement, impairment and derecognition of financial assets and liabilities, as well as general hedge accounting. The adoption of IFRS 9 has had no significant impact on the Company's interim financial statements.

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

These financial statements were authorized for issue by the Company's Board of Directors on July 25, 2018.

Accounting Standards Issued and Not Applied

In January 2016, the International Accounting Standards Board 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 a depreciation expense for right-of-use assets and interest expense on lease liabilities.

It is expected that IFRS 16 will have an impact on the Company's financial statements with recognition of new assets and liabilities for its operating leases. The Company is still in the process of assessing the quantitative impact on its financial statements of this new standard. The Company's future minimum lease payments, on an undiscounted basis, under non-cancellable operating leases at December 31, 2017 were $42.5 million.

2. Seasonality of Operations

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 and pulp mills. Market demand also varies seasonally to some degree. For example, building activity and repair and renovation work, which affect demand for solid wood products, are generally stronger in the spring and fall months. Shipment volumes are affected by these factors as well as by global supply and demand conditions.

3. Inventories

(millions of Canadian dollars, unaudited)		**As at June 30, 2018**		As at December 31, 2017
Logs	**$**	**121.9**	$	132.1
Finished products		**366.5**		354.6
Residual fibre		**23.8**		20.8
Materials and supplies		**125.4**		121.4
	$	**637.6**	$	628.9

Inventory balances are stated after inventory write-downs from cost to net realizable value. There were no inventory write-downs at June 30, 2018 or December 31, 2017.

4. Long-Term Investments and Other

(millions of Canadian dollars, unaudited)		**As at June 30, 2018**		As at December 31, 2017
Investments	**$**	**23.6**	$	22.5
Duties receivable		**71.9**		44.9
Other deposits, loans and advances		**9.5**		15.9
	$	**105.0**	$	83.3

The duties receivable balance represents US dollar anti-dumping and countervailing duty cash deposits paid in excess of the calculated expense accrued at June 30, 2018 (Note 14).

5. Operating Loans and Long-Term Debt

(a) Available Operating Loans

(millions of Canadian dollars, unaudited)		**As at June 30, 2018**		As at December 31, 2017
Canfor (excluding CPPI)				
Available Operating Loans:				
Operating loan facilities	**$**	**350.0**	$	350.0
Facilities for letters of credit		**60.0**		50.0
Total operating loan facilities		**410.0**		400.0
Letters of credit		**(56.1)**		(44.0)
Total available operating loan facilities - Canfor	**$**	**353.9**	$	356.0
CPPI				
Available Operating Loans:				
Operating loan facility	**$**	**110.0**	$	110.0
Letters of credit		**(10.8)**		(9.2)
Total available operating loan facility - CPPI	**$**	**99.2**	$	100.8
Consolidated:				
Total operating loan facilities	**$**	**520.0**	$	510.0
Total available operating loan facilities	**$**	**453.1**	$	456.8

Interest is payable on Canfor's operating loans at floating rates based on the lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin that varies with the Company's debt to total capitalization ratio.

On April 6, 2018, the maturity date of CPPI's principal operating loan facility was extended from January 31, 2020 to April 6, 2022. The terms of CPPI'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 lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin. Canfor's principal operating loan facility has a maturity date of September 28, 2022.

Both Canfor's and CPPI's operating loan facilities have certain financial covenants, including maximum debt to total capitalization ratios. No amounts were drawn on the Company's operating loan facilities as at June 30, 2018 (December 31, 2017 - nil).

Canfor (excluding CPPI) has separate facilities to cover letters of credit. At June 30, 2018, $53.6 million of letters of credit outstanding are covered under these facilities with the balance of $2.5 million covered under Canfor's general operating loan facility.

On February 28, 2018, the Company increased one of its letter of credit facilities by $10.0 million, which can be drawn in either Canadian or US dollars.

As at June 30, 2018, the Company and CPPI were in compliance with all covenants relating to their operating loans. Substantially all borrowings of CPPI are non-recourse to other entities within the Company.

(b) Long-Term Debt

All borrowings of the Company feature similar financial covenants, including a maximum debt to total capitalization ratio.

As at June 30, 2018, the Company was in compliance with all covenants relating to its long-term debt.

Fair value of total long-term debt

At June 30, 2018, the fair value of the Company's long-term debt is $394.2 million (December 31, 2017 - $389.1 million). The fair value was determined based on prevailing market rates for long-term debt with similar characteristics and risk profile.

6. Employee Future Benefits

For the three months ended June 30, 2018, defined benefit plan actuarial gains of $2.0 million (before tax) were recognized in other comprehensive income (loss), principally reflecting the return generated on plan assets. For the six months ended June 30, 2018, gains of $15.2 million (before tax) were recognized in other comprehensive income (loss). For the three and six months ended June 30, 2017, the Company recognized before tax actuarial losses in other comprehensive income (loss) of $35.2 million and $31.9 million, respectively.

The discount rate assumptions used to estimate the changes in net retirement benefit obligations were as follows:

	Defined Benefit Pension Plans	**Other Benefit Plans**
June 30, 2018	**3.6%**	**3.6%**
March 31, 2018	3.6%	3.6%
December 31, 2017	3.4%	3.4%
June 30, 2017	3.5%	3.5%
March 31, 2017	3.9%	3.9%
December 31, 2016	3.9%	3.9%

7. Financial Instruments

The Company's financial assets are measured at amortized cost with the exception of certain investments in equity interests, which are measured at fair value through profit and loss. Financial liabilities are measured at amortized cost with the exception of certain derivative instruments, which are measured at fair value through profit and loss.

IFRS 13 *Fair Value Measurement,* requires classification of financial instruments 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, either directly or indirectly;

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

The following table summarizes Canfor's financial instruments measured at fair value at June 30, 2018 and December 31, 2017, and shows the level within the fair value hierarchy in which the financial instruments have been classified:

(millions of Canadian dollars, unaudited)	Fair Value Hierarchy Level		**As at June 30, 2018**		As at December 31, 2017
Financial assets measured at fair value					
Investments	Level 1	**$**	**23.1**	$	21.8
Financial liabilities measured at fair value					
Derivative financial instruments	Level 2	**$**	**5.8**	$	0.8

The Company uses a variety of derivative financial instruments, which are included in Level 2 of the fair value hierarchy, to reduce its exposure to risks associated with fluctuations in foreign exchange rates, lumber prices, energy prices, and floating interest rates on long-term debt.

The fair value of these financial instruments was determined based on prevailing market rates for instruments with similar characteristics.

The following table summarizes the gain (loss) on derivative financial instruments for the three and six-month periods ended June 30, 2018 and 2017:

	3 months ended June 30,				6 months ended June 30,			
(millions of Canadian dollars, unaudited)		**2018**		2017		**2018**		2017
Energy derivatives	**$**	**-**	$	-	**$**	**(0.1)**	$	-
Lumber futures		**(7.6)**		-		**(15.5)**		3.2
Gain (loss) on derivative financial instruments	**$**	**(7.6)**	$	-	**$**	**(15.6)**	$	3.2

8. Income Taxes

	3 months ended June 30,				6 months ended June 30,			
(millions of Canadian dollars, unaudited)		**2018**		2017		**2018**		2017
Current	**$**	**(61.2)**	$	(35.5)	**$**	**(118.0)**	$	(60.6)
Deferred		**(10.6)**		3.0		**(4.5)**		0.3
Income tax expense	**$**	**(71.8)**	$	(32.5)	**$**	**(122.5)**	$	(60.3)

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

	3 months ended June 30,				6 months ended June 30,			
(millions of Canadian dollars, unaudited)		**2018**		2017		**2018**		2017
Income tax expense at statutory rate – 27% (2017 – 26.0%)	**$**	**(73.0)**	$	(32.1)	**$**	**(124.9)**	$	(59.5)
Add (deduct):								
Entities with different income tax rates and other tax adjustments		**1.6**		(0.7)		**3.2**		(1.9)
Non-taxable income related to non-controlling interests		**0.1**		0.1		**0.2**		0.2
Permanent difference from capital gains and losses and other non-deductible items		**(0.5)**		0.2		**(1.0)**		0.9
Income tax expense	**$**	**(71.8)**	$	(32.5)	**$**	**(122.5)**	$	(60.3)

In addition to the amounts recorded to net income, a tax expense of $0.5 million was recorded to other comprehensive income (loss) for the three months ended June 30, 2018 in relation to the actuarial gains on defined benefit plans (three months ended June 30, 2017 - tax recovery of $9.2 million). For the six months ended June 30, 2018, the tax expense was $4.1 million (six months ended June 30, 2017 - tax recovery of $8.3 million).

Also included in other comprehensive income (loss) for the three months ended June 30, 2018 was a tax expense of $0.8 million related to foreign exchange differences on translation of investments in foreign operations (three months ended June 30, 2017 - tax recovery of $1.0 million). For the six months ended June 30, 2018, the tax expense was $1.8 million (six months ended June 30, 2017 - tax recovery of $1.3 million).

Subsequent to quarter-end, the Company made 2018 income tax instalment payments of $61.6 million.

9. Earnings Per Share and Normal Course Issuer Bid

Basic net income per share is calculated by dividing the net income attributable to common equity shareholders by the weighted average number of common shares outstanding during the period.

	3 months ended June 30,		6 months ended June 30,	
	2018	2017	**2018**	2017
Weighted average number of common shares	**128,625,480**	132,804,543	**128,625,694**	132,804,543

On March 5, 2018, the Company renewed its normal course issuer bid whereby it can purchase for cancellation up to 6,439,764 common shares or approximately 5% of its issued and outstanding common shares as of March 1, 2018. The renewed normal course issuer bid is set to expire on March 6, 2019. During the three months ended June 30, 2018, the Company did not purchase any common shares. During the six months ended June 30, 2018, the Company purchased 19,500 shares for $0.5 million (an average of $25.64 per common share), and paid an additional $3.7 million in relation to shares purchased in the prior year. As at June 30, 2018 and July 25, 2018, there were 128,625,480 common shares of the Company outstanding.

Under a separate normal course issuer bid, CPPI purchased 500 common shares in the six months ended June 30, 2018 at an average of $13.01 per common share from non-controlling shareholders, and paid an additional $0.1 million in relation to shares purchased in the prior year. During the three months ended June 30, 2018, CPPI did not purchase any common shares. As at June 30, 2018 and July 25, 2018, Canfor’s ownership interest in CPPI was 54.8%.

10. Net Change in Non-Cash Working Capital

	3 months ended June 30,		6 months ended June 30,	
(millions of Canadian dollars, unaudited)	**2018**	2017	**2018**	2017
Accounts receivable	**$ (51.1)**	$ 27.8	**$ (102.6)**	$ (36.4)
Inventories	**134.8**	100.7	**(4.9)**	(9.2)
Prepaid expenses and other	**(8.1)**	(8.7)	**(25.5)**	(14.3)
Accounts payable, accrued liabilities and current portion of deferred reforestation obligations	**(13.7)**	(27.5)	**42.8**	47.0
Net decrease (increase) in non-cash working capital	**$ 61.9**	$ 92.3	**$ (90.2)**	$ (12.9)

11. Segment Information

Canfor has two reportable segments (lumber segment and pulp and paper segment), which offer different products and are managed separately because they require different production processes and marketing strategies.

Sales between segments are accounted for at prices that approximate fair value. These include sales of residual fibre from the lumber segment to the pulp and paper segment for use in the pulp production process.

The Company's panels business does not meet the criteria to be reported fully as a separate segment and is included in Unallocated & Other below.

(millions of Canadian dollars, unaudited)		Lumber		Pulp & Paper		Unallocated & Other		Elimination Adjustment		Consolidated
3 months ended June 30, 2018										
Sales to external customers	**$**	**1,063.2**	**$**	**396.3**	**$**	**-**	**$**	**-**	**$**	**1,459.5**
Sales to other segments		**62.1**		**0.1**		**-**		**(62.2)**		**-**
Operating income (loss)		**203.4**		**85.4**		**(6.7)**		**-**		**282.1**
Amortization		**47.9**		**19.7**		**-**		**-**		**67.6**
Capital expenditures[1]		**61.8**		**24.8**		**1.0**		**-**		**87.6**
3 months ended June 30, 2017										
Sales to external customers	$	878.7	$	280.9	$	-	$	-	$	1,159.6
Sales to other segments		41.9		-		-		(41.9)		-
Operating income (loss)		110.4		31.5		(10.9)		-		131.0
Amortization		43.6		18.5		-		-		62.1
Capital expenditures[1]		41.7		19.2		0.8		-		61.7
6 months ended June 30, 2018										
Sales to external customers	**$**	**1,937.1**	**$**	**755.9**	**$**	**-**	**$**	**-**	**$**	**2,693.0**
Sales to other segments		**112.2**		**0.2**		**-**		**(112.4)**		**-**
Operating income (loss)		**329.3**		**170.5**		**(13.9)**		**-**		**485.9**
Amortization		**93.5**		**38.9**		**-**		**-**		**132.4**
Capital expenditures[1]		**94.9**		**44.6**		**4.5**		**-**		**144.0**
Identifiable assets		**2,413.4**		**872.5**		**707.8**		**-**		**3,993.7**
6 months ended June 30, 2017										
Sales to external customers	$	1,674.8	$	590.0	$	-	$	-	$	2,264.8
Sales to other segments		82.8		0.1		-		(82.9)		-
Operating income (loss)		194.1		66.7		(23.0)		-		237.8
Amortization		87.1		37.3		-		-		124.4
Capital expenditures[1]		61.6		36.0		3.0		-		100.6
Identifiable assets		2,254.2		793.2		350.5		-		3,397.9

[1]Capital expenditures represent cash paid for capital assets during the periods. Pulp & Paper includes capital expenditures by CPPI that were partially financed by government grants.

12. Acquisitions

(a) US South

On January 2, 2015, the Company completed the first phase of the acquisition of Beadles Lumber Company & Balfour Lumber Company Inc. ("Beadles & Balfour") for total consideration of $51.6 million (US$44.0 million), representing an initial 55% interest.

On January 2, 2017, the Company completed the final phase of the acquisition of Beadles & Balfour for $41.8 million (US$31.1 million) bringing Canfor's interest in Beadles & Balfour to 100%. Upon completion of the final phase of the acquisition, the forward purchase liability of $41.8 million and non-controlling interest of $19.9 million were derecognized, and $36.5 million was recorded in other equity. In addition, $16.6 million was charged to retained earnings reflecting Canfor's election to account for the non-controlling interest related to Beadles & Balfour as the non-controlling share of the fair value of the net identifiable assets at the acquisition date.

The acquisition was accounted for in accordance with IFRS 3, *Business Combinations*.

(b) Wynndel Box and Lumber Ltd.

On April 15, 2016, the Company completed the acquisition of the assets of Wynndel Box and Lumber Ltd. ("Wynndel") for total consideration of $40.3 million. The acquisition was accounted for in accordance with IFRS 3, *Business Combinations*.

At the acquisition date, the Company paid $19.7 million, and a working capital true-up payment of $2.6 million was paid in early July 2016. On April 5, 2017, the Company paid an instalment of $14.4 million, and the final instalment of $3.6 million was paid on October 15, 2017.

13. Change in Ownership Interest in Canfor Energy North Limited Partnership

On January 1, 2018, Pacific BioEnergy Corporation ("PBEC") exercised its option to purchase from Canfor an additional 10% of the outstanding shares of Canfor Energy North Limited Partnership ("CENLP") for consideration of $3.5 million, which was received in December 2017, thereby increasing their ownership from approximately 5% to 15%.

Accordingly, the non-controlling interest of CENLP was increased by $2.5 million to reflect PBEC's 15% total ownership from January 1, 2018 onwards. A net gain of $1.3 million was recorded as a credit to equity in the first quarter of 2018 representing the difference between the adjustment to Canfor's investment in CENLP and the consideration paid, and the associated tax effects.

14. Countervailing and Anti-Dumping Duties

On November 25, 2016, a petition was filed by the US Lumber Coalition to the US Department of Commerce ("DOC") and the US International Trade Commission ("ITC") alleging certain subsidies and administered fees below the fair market value of timber that favour Canadian lumber producers, an assertion the Canadian industry and Provincial and Federal Governments strongly deny and have successfully disproven in international courts in the past. Canfor was selected by the DOC as a "mandatory respondent" to the countervailing and anti-dumping investigations and is subject to company specific countervailing and anti-dumping duties.

On April 24, 2017, the DOC announced its preliminary countervailing duty ("CVD") of 20.26% specific to Canfor, to be posted by cash deposits or bonds on the exports of softwood lumber to the US effective April 28, 2017 to August 25, 2017. Following this period, CVD duties were not applicable on lumber shipments destined to the US from August 26, 2017 to December 27, 2017. On June 23, 2017, the DOC announced its preliminary anti-dumping duty determination ("ADD") of 7.72% specific to Canfor, to be posted by cash deposits or bonds on the exports of softwood lumber to the US effective June 30, 2017.

Final countervailing and anti-dumping duty determinations were announced by the DOC on November 2, 2017, while the ITC issued an affirmative determination of injury on December 7, 2017. As a result, Canfor was issued a final ADD rate of 7.28% effective November 8, 2017, and was subject to countervailing duties on Canadian lumber exports destined to the US at a reduced rate of 13.24%, effective December 28, 2017. Notwithstanding the final rates established in the DOC's investigation, the final liability for the assessment of CVD and ADD will not be determined until an official administrative review of the respective period is complete. For the CVD rate, the first period of review will be based on sales and cost data through 2017 and 2018, with the ADD rate based off data from July 2017 to December 2018. The first period of review is currently anticipated to be completed in 2020.

In the second quarter of 2018, cash deposits were posted reflecting the final published ADD rate of 7.28% and CVD rate of 13.24% as determined by the DOC; however for accounting purposes, the ADD expense is being accrued at 1.7% reflecting Canfor's best estimate of the ADD rate applicable to its product shipment profile, as determined by applying the DOC's methodology to current sales and cost data. The estimated ADD rate at June 30, 2018 increased 0.6% from the estimated rate on March 31, 2018. Canfor is unable to determine a current CVD accrual rate for accounting purposes, and therefore has recorded an expense at the CVD deposit rate.

Canfor will continue to reassess its estimate of the ADD rate at the end of each quarter in 2018 by applying the DOC's methodology to updated sales and cost data as this becomes available. These estimates may result in a material adjustment to the Income Statement on a quarterly basis during the first period of review. Accordingly, Canfor has recorded a receivable of $71.9 million (Note 4) reflecting the difference between the current combined cash deposit rate of 20.52% and the current combined accrual rate for accounting purposes of 14.94%.

Canfor and other Canadian forest product companies, the Federal Government and Canadian Provincial Governments categorically deny the US allegations and strongly disagree with the current countervailing and anti-dumping determinations made by the DOC. Canada has proceeded with legal challenges under NAFTA and through the World Trade Organization, where Canadian litigation has proven successful in the past.