**FROM THE SEEDS OF ADVERSITY**

**COMES GREAT STRENGTH**

CANFOR CORPORATION

CANFOR

ANNUAL REPORT 2008

## COMPANY OVERVIEW

Canfor is a leading integrated forest products company based in Vancouver, British Columbia (B.C.) with interests in 31 facilities in B.C., Alberta, Quebec, Washington State, and North and South Carolina. The company produces the most softwood lumber in Canada, while also producing oriented strand board (OSB), plywood, remanufactured lumber products and specialized wood products. Canfor shares are traded on the Toronto Stock Exchange under the symbol CFP. The main operating company is Canadian Forest Products Ltd., from which the name is derived.

Canfor also owns a 50.2% interest in Canfor Pulp Limited Partnership, which is one of the largest producers of northern softwood kraft pulp in Canada and a leading producer of high performance kraft paper.

Canfor has an annual production capability of approximately 5 billion board feet of lumber, 270 million square feet of plywood, and 1 billion square feet of OSB. Canfor also has approximately 11 million cubic meters of allowable annual cut under its forest tenures, 96% of which is CSA SFM certified.

## OUR PRODUCTS

### SPF LUMBER

Dimension Lumber
Studs (Solid & Finger Joined)
Long Length Finger Joined Lumber
Added Value and Industrial Products

Dimension Lumber

### STRUCTURAL PANELS

Plywood
OSB

Plywood

### SYP LUMBER

Dimension Lumber
Studs (Solid & Finger Joined)
Added Value and Industrial Products

SYP Lumber

### SILVASTAR

Fascia and Trim
Decking
Log Cabin Siding
Pattern Stock
Furring Strips

Fascia

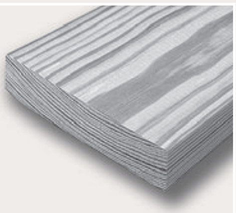
### ENGINEERED LUMBER

MSR
Long Length Finger Joined MSR

MSR

### GATOR GUARD

Treated Lumber
Treated Plywood
Treated Siding
Treated Balusters
Treated Spindles



Treated Lumber

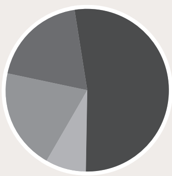
## FINANCIAL HIGHLIGHTS

| | | 2008 | 2007 |
|---|---|---|---|
| **Sales and income** (millions of dollars) | Sales | $ 2,611.6 | $ 3,275.6 |
| | Operating income (loss) | $ (158.1) | $ (273.0) |
| | Asset impairments | $ (169.6) | $ (268.0) |
| | Net income (loss) | $ (345.2) | $ (360.6) |
| Per common share (dollars) | Net income (loss) | $ (2.42) | $ (2.53) |
| | Book value | $ 10.48 | $ 12.74 |
| | Share price | | |
| | High | $ 11.06 | $ 13.74 |
| | Low | $ 5.96 | $ 7.64 |
| | Close – December 31 | $ 7.60 | $ 8.73 |
| | Common shares outstanding - December 31 | 142,589,312 | 142,589,312 |
| Financial position (millions of dollars) | Working capital | $ 531.4 | $ 815.2 |
| | Total assets | $ 3,200.4 | $ 3,507.8 |
| | Long-term debt | $ 428.7 | $ 481.6 |
| | Common shareholders' equity | $ 1,494.8 | $ 1,817.1 |
| | Total capitalization | $ 2,651.5 | $ 3,104.2 |
| **Additional information** [1] | Return on capital employed | (16.4)% | (15.6)% |
| | Return on common shareholders' equity | (18.5)% | (17.8)% |
| | Ratio of current assets to current liabilities | 2.0 : 1 | 3.0 : 1 |
| | Ratio of net debt to capitalization | 15% | 10% |
| | EBITDA (millions of dollars) | $ 13.1 | $ (88.9) |
| | EBITDA margin | 0.5% | (2.7)% |
| | Capital expenditures (millions of dollars) | $ 80.2 | $ 90.6 |

(1) See Definitions of Selected Financial Terms on page 84.

### SALES BY MARKET 2008

- USA 53%
- Canada 19%
- Far East 20%
- Europe & Other 8%



### SALES BY PRODUCT LINE 2008

- Lumber 47%
- Pulp & Kraft Paper 36%
- Plywood & OSB 6%
- Resale Lumber 2%
- Miscellaneous 9%


In 2008, Canfor celebrated 70 years as a company. With experience comes strength. For seven decades, we have consistently and successfully responded to market pressures as well as opportunities. This capacity to adapt, evolve and most importantly improve is ingrained in everything we do.

As we mark this important milestone, we will highlight some of the valuable experiences that have prepared us for today and formed the foundation for our vision for tomorrow.

In the last year, we have worked diligently to face the challenges within our industry, and we stand confident in our ability to emerge from difficult times stronger than ever.

## PRESIDENT'S MESSAGE TO SHAREHOLDERS

At a time like this, I would expect that you would have a keen interest in the current and future plans of Canfor management. Like you, I have seen my share value drop over the past two years and, as a shareholder, I am not too happy about this result.

Having said that, I feel it is especially important that you fully understand the situation at Canfor and where Canfor stands in the industry.

The local headlines report daily on the declining lumber markets, so you are aware of the challenge that is presented to us by the global economy. It is small comfort to say that our industry was the first to feel the effect of this economic tsunami, but this fact is relevant because the housing sector may be the area where the recovery will begin.

While the timing of the recovery is unclear, looking longer term, this industry will be a good place for investment. Why? Because up until now the only reason that lumber prices grew on thriving economies was not due to lack of supply, but because the velocity of increased production just couldn't match the demands of a strong global economy. Those days are just about over.

The timber supply in British Columbia and possibly in Alberta will shrink in the future as a result of the Mountain Pine Beetle epidemic. In Quebec and Ontario the annual allowable harvest has been significantly reduced to ensure that future harvesting is at sustainable levels. This will coincide with a growing appetite for our lumber not only from our North American consumers, but also from Japan and our emerging markets in South East Asia, especially China. In other words, our industry will soon be providing a highly-valued commodity that will be in short supply. This should lead to healthy price stability and favorable investment returns for shareholders.

I am happy to report that our relentless commitment to cash conservation has seen us finish 2008 with a cash balance of $362 million, which is more than our balance at the end of 2007. With this balance, our continued focus on cost containment and a healthy credit line, we are well-positioned to take advantage of the opportunities that will appear when the economy recovers.

How, you may ask, has Canfor been able to maintain such a strong relative position in such a poor market? The answer is alignment. Alignment with an experienced and business-wise board of directors, a focused management team and a dedicated workforce all striving to make Canfor the dominant global supplier of wood product solutions to our highly valued customers.

Starting in mid-2007, we launched a company-wide cost reduction effort. This included a 25% reduction of our head office and support functions and a rollback of salaries, including 25% for me as CEO, 15% for our Executive, 7% for management and 3% for all other salaried employees. We asked all of our suppliers and contractors for a 15% reduction in fees and we sold the corporate jet, which removed an annual expense of $2 million. To support management's efforts, the Company's Board of Directors elected to rollback their fees by 50% up from 33% in 2007.

In 2008, we further intensified our efforts, reducing our manufacturing costs by 12% year over year. Through all of this we have taken a large quantity of product off the market with the indefinite closures of our Polarboard, Tackama, Chetwynd and Mackenzie mills. Additionally, we have taken significant curtailments across the company in BC, Alberta, and North and South Carolina. This has reduced our output by 30% from our total capacity. Despite all of these measures, we have continued to provide our highly-valued customers with a high quality product in the right profile and in a timely manner.

We continue to closely monitor our markets, our inventories and our cost base. I can assure you the Canfor management team is highly capable and committed to steering this company through this economic storm to the calmer waters of a healthy economy. Until then let me assure you, my fellow shareholders, that our team is applying enlightened management principles with a tight-fisted approach to cash conservation and a strategic awareness of the opportunities and challenges that lie ahead.

I wish to conclude my remarks by expressing appreciation to all of our employees who are working to make this company even stronger going forward. My thanks to all board members for their wise counsel and to all management for their capable and committed leadership. Finally, to our highly-valued customers who have been so helpful and loyal, I wish to extend a sincere thank you.

Jim Shepard
President and
Chief Executive Officer


"...the company is in sound financial shape with one of the best balance sheets in our industry."

## CHAIRMAN'S MESSAGE TO SHAREHOLDERS

This will be my final report to shareholders as Chairman of Canfor Corporation. Canfor has been a very important part of my life since my family founded the predecessor company in 1938.

2008 was probably the most difficult year in our Company's history, which isn't the best way to celebrate our 70th Anniversary.

Although the outlook for the current year is very difficult, the company is in sound financial shape with one of the best balance sheets in our industry. It has great leadership in our President, Jim Shepard, and he has an excellent team to support him.

It has been my privilege to work with so many wonderful people throughout the years. They are not just business associates but personal friends. Canfor is truly a people company. We care about our customers, our suppliers and the environment; however, most importantly, we care about our employees and their safety. Canfor has dedicated and loyal employees and I want to thank them all for their efforts.

Since becoming a public company in 1983, we have been privileged to have highly qualified people serving on the Company's Board. I want to thank both the present as well as all former Directors for their advice and input.

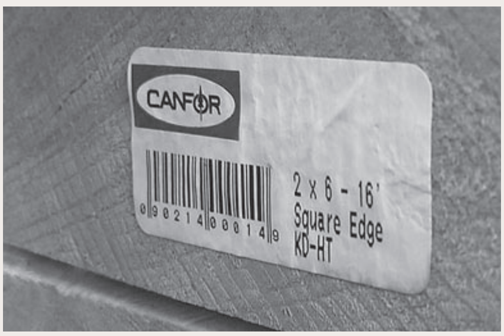
I have decided to step down at this time because I have a health issue called Myasthenia Gravis, which at times makes it difficult for me to speak. I am not saying farewell because I will remain on the Board and will continue to be totally dedicated to the future success of Canfor. Times will get better; Canfor will not only survive but will go on to be a highly successful major player in the global forest products industry.

Peter Bentley
Chairman of the Board


# ADAPT

Key to surviving market fluctuations is the ability to adapt to changing circumstances. In response to the unprecedented downturn in the economy, we initiated Project Endurance. Engaging employees, suppliers and contractors, we reduced costs while still meeting or exceeding key customer needs. We remain committed to further cost reductions, as we adapt to the changing landscape of our industry.

Responsiveness is key to Canfor's strategy. In the early 1980s, during a previous market downturn, we responded by initiating a customer-centric model that would guide the company to this day. **Vendor-managed inventories** and **bar-coding lumber** are just two of the highlights that, although now commonplace, were instrumental in nurturing lasting relationships with our highly-valued customers.




# EVOLVE

**An integral part of our evolution is our ability to seek out new operating areas and new markets. With U.S. housing starts at record lows, 2008 forced the forest industry to look to other markets for relief. With a regional office in China, we are well-positioned to take advantage of this emerging market.**

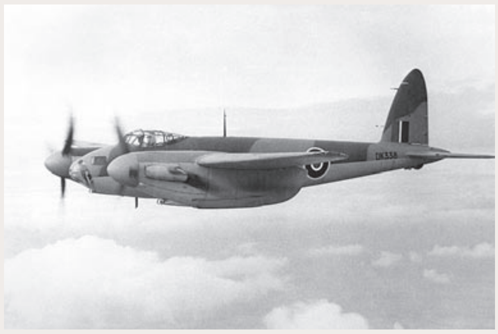
In early 2009, the Shanghai government formally approved a B.C.-designed wood roofing system as part of a plan to renovate 10,000 apartment buildings. As well, our participation in a trade mission to China in the fall of 2008 resulted in new business and increased support for wood frame construction. 2008 also saw the construction of a school built entirely of Canfor wood in China's Sichuan province.

Closer to home, we expanded our presence in the United States in 2006, with the purchase of New South Companies Inc.

While we have had a presence in Japan for many decades, we established our present day regional office in 2003.

All Mosquito Bombers that ever flew, except for the prototype, used our plywood.

Our first major push to conquer new territory began in 1963 when we expanded into the northern British Columbia interior. Purchasing timber rights and several sawmills, the company moved its focus away from the coastal forest industry.



We also sought innovative applications for our products. One of the most interesting products we produced earned the name "The Timber Terror." In 1940, Canfor produced aircraft plywood for the Mosquito Bomber, which flew countless missions in WWII. All Mosquito Bombers that ever flew, except for the prototype, used our plywood.

# IMPROVE

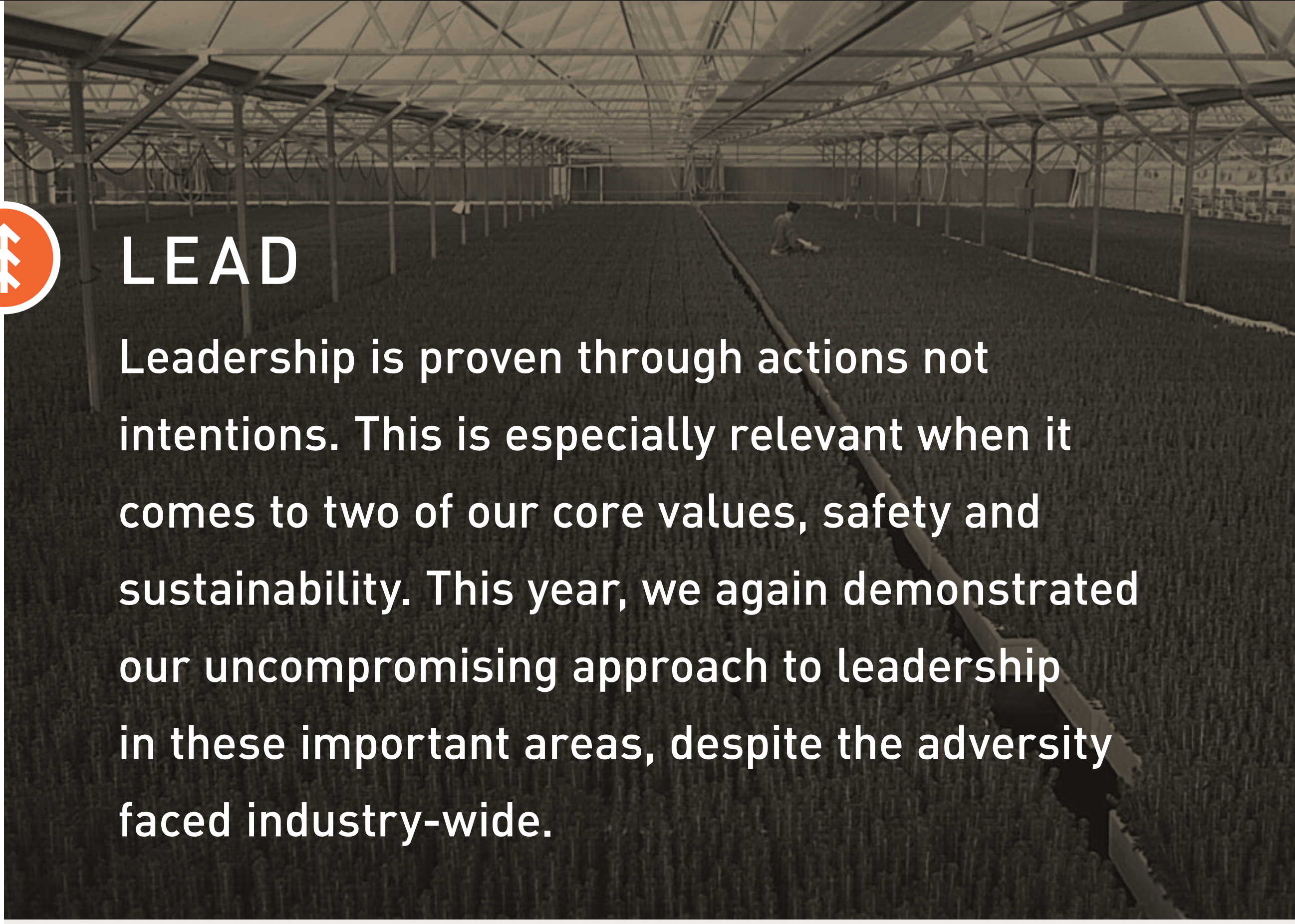
A strong commitment to improving the way we operate is a cornerstone of our business model. We recognize that a company's greatest strength is its employees. Undertaking an ambitious plan to fundamentally change the way the forest products industry operates, we have implemented a continuous improvement program that touches every aspect of the business, including woodlands, mills, human resources, sales and our head office.

By engaging our employees and harnessing their expertise, ideas and efforts, we will improve the performance of our business.

A formal approach to improvement at Canfor began in 1973. Instituting a program called Better Methods, we placed mill supervisors in classrooms giving them leadership and business skills.

Of course the end goal of any improvement initiative is quality. Upgrading our training methods and the way we operate has translated into a quality product that our customers seek out over that of our competitors.

With some of the highest quality standards for our lumber, we've developed strong relationships with key customers. Those relationships are serving us well through this current downturn, as they provide a stable source of demand for our product.



# LEAD

**Leadership is proven through actions not intentions. This is especially relevant when it comes to two of our core values, safety and sustainability. This year, we again demonstrated our uncompromising approach to leadership in these important areas, despite the adversity faced industry-wide.**

## SAFETY

"Safety comes first at Canfor." This isn't just our motto, it is the underlying foundation of everything we've done for the past 70 years. Developing and evolving our safety approaches and processes helps us to constantly learn how to make our business safer. In 2008, we had our lowest injury rate ever. The commitment to safety is even more important during a market downturn, as our employees try to maintain focus despite much uncertainty. This makes our achievements in reducing the number of incidents this year even more remarkable. In 2008, the injury rate in our sawmills was less than half of the rest of the industry.

> In 2008, the injury rate in our sawmills was less than half of the rest of the industry.

## SUSTAINABILITY

Despite our determination to reduce costs in the face of the most challenging economic conditions in decades, one area where we did not sacrifice was sustainability. In 2008, we maintained all of our requirements for sustainable forest management and silviculture. We also completed PEFC Chain of Custody certification for our operating mills in Western Canada, which means we are able to track our products from the forest, through all stages of production, to the final customer as an end product. This is becoming increasingly important to our customers, who require that their wood products supply does not come from controversial sources. Because we plant 3 trees for every 1 tree harvested and their survival rate is at least 90%, we are ensuring the sustainability of our forests long term.

Throughout our history, we have defined ourselves through our leadership in sustainability. We were one of the first forest products companies in Western Canada to publish a stand alone environment report, eventually becoming what is now our annual sustainability report. This year, we take our report one step further by directing you to our website in the interest of further environmental responsibility. Our report can be found at **www.canfor.com/sustainability.**

# MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") provides a review of Canfor's financial performance for the year ended December 31, 2008 relative to the year ended December 31, 2007, and the financial position of the Company. It should be read in conjunction with Canfor's Annual Information Form and its audited consolidated financial statements and accompanying notes for the years ended December 31, 2008 and 2007. The financial information contained in this MD&A has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

Throughout this discussion, reference is also made to EBITDA (calculated as operating income before amortization) and Adjusted EBITDA (calculated as EBITDA less restructuring, mill closure and severance costs), which Canfor considers to be important indicators 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 Net Loss (calculated as Net Loss less specific items affecting comparability with prior periods – for the full calculation, see reconciliation included in the section "Overview of Consolidated Loss – 2008 Compared to 2007") and Adjusted Net Loss per Share (calculated as Adjusted Net Loss divided by the weighted average number of shares outstanding in the period). EBITDA, Adjusted EBITDA, Adjusted Net Loss and Adjusted Net Loss 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 Canadian GAAP. As there is no standardized method of calculating these measures, Canfor's EBITDA, Adjusted EBITDA, Adjusted Net Loss and Adjusted Net Loss per Share may not be directly comparable with similarly titled measures used by other companies. Reconciliations of EBITDA, Adjusted EBITDA and Adjusted Net Loss to net income reported in accordance with GAAP are included in this MD&A.

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

Certain prior period comparative information throughout this report has been restated for consistency with the presentation in the current period. All financial references are in millions of Canadian dollars unless otherwise noted. The information in this report is as at February 19, 2009.

**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.

## OVERVIEW OF 2008

2008 was a most difficult year for Canfor's lumber business. With the industry already facing a severe and prolonged U.S. housing market downturn, producers were dealt a further blow later in the year as the emerging crisis in global financial and credit markets and a worsening of the U.S. economy weighed heavily on the sector. By the end of 2008, seasonally adjusted annual U.S. housing starts had plunged to 550,000 units, the lowest level on record, and lumber prices were languishing at the lowest level in decades. Market conditions for oriented strand board ("OSB") and plywood products fared little better in 2008, with prices remaining at depressed levels through much of the year. Pulp markets too, after a strong start to the year, failed to escape the fallout from the financial and credit market upheaval and contraction in demand, with prices falling sharply later in the year as pulp inventories mounted.

Compounding the challenges for Canadian lumber producers was a 15% export tax on shipments to the United States that continued through 2008. The one positive development for Canadian producers was the sharp depreciation of the Canadian dollar relative to its U.S. counterpart in the fourth quarter of 2008 which helped to mitigate the erosion of Canadian dollar sales realizations. The average value of the Canadian dollar in 2008, however, remained relatively unchanged relative to the US dollar compared to 2007.

The Company significantly reduced its solid wood production levels during 2008 to reflect the substantially lower demand, indefinitely idling two lumber mills and two panel plants (one OSB and one plywood) in the British Columbia ("B.C.") Interior, and reducing shifts and operating shortened work weeks at its other operations. Further loss of production resulted from a fire in May of 2008, which destroyed the Company's North Central Plywoods ("NCP") facility.

At year end, the Company was producing at less than 75% of its total lumber production capacity, and at a fraction of its panels capacity. Due to the market conditions and closures, the Company recorded further asset impairment charges on its panel assets at the end of 2008.

Notwithstanding the various market challenges, Canfor recorded a significantly improved operational performance in 2008, and ended the year with one of the strongest balance sheets in the industry. Manufacturing costs were significantly reduced in 2008, mostly through successful performance improvement initiatives and cost control measures. As a result of this improved performance, combined with tight management of working capital and non-essential capital expenditures, the Company ended the year with cash of $362.4 million.

A brief review of the more significant developments in 2008 is presented below.

## DEPRESSED HOUSING MARKET AND HISTORICALLY-LOW PRICES

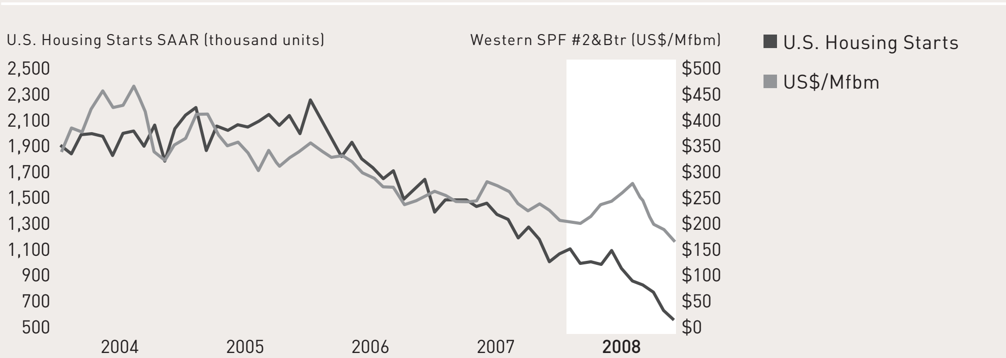
### i. DEPRESSED MARKET CONDITIONS AND PRICES

Reflecting the deterioration of the U.S. economy, eroding consumer confidence and spending, and high unsold home inventories, U.S. housing starts plunged in 2008 to the lowest level since records began in 1959. U.S. housing starts in 2008 were 902,000 units[1], a 33% decrease from the 2007 total of 1.341 million units. Most disconcerting, however, was the almost 50% decline in housing starts between the beginning and end of 2008, and the lowest level of housing starts on record at 550,000 (Seasonally Adjusted Annual Rates – SAAR) in December. Inventories of new and used homes available for sale in the U.S. market in December of 2008 were 12.9 months and 9.3 months[2], respectively, well above historical levels. Compared to new home construction, the Repair and Remodeling and Do-It-Yourself sector fared a little better, recording more modest declines in 2008 although demand for lumber fell off sharply towards the end of the year.

For lumber, Western Spruce/Pine/Fir ("SPF") 2x4 #2&Btr prices, which started the year at US$219 per Mfbm, a historically low level, dipped to US$190 per Mfbm in the first quarter before increasing slowly but steadily as supply tightened to reach US$283 per Mfbm[3] in August. However, this high was short-lived as prices fell dramatically through the balance of the year in response to the worsening economic climate and resulting slump in demand to end the year at US$168 per Mfbm. The 2008 annual average Random Length price of Western SPF 2x4 #2&Btr was US$222 per Mfbm, an 11% decline compared to the 2007 annual average, while price declines for wider widths were as high as 22%. The average price of Southern Yellow Pine ("SYP") 2x4 East was US$281 per Mfbm[3], almost unchanged from 2007; however, prices for wider width product recorded significant year-over-year decreases, as evidenced by a 16% decline in the average 2x10 Random Length price.

The following chart highlights the significant downward trend in U.S. housing starts and monthly average Western SPF 2x4 #2&Btr benchmark lumber prices in 2008:

LUMBER PRICE COMPARED TO U.S. HOUSING STARTS



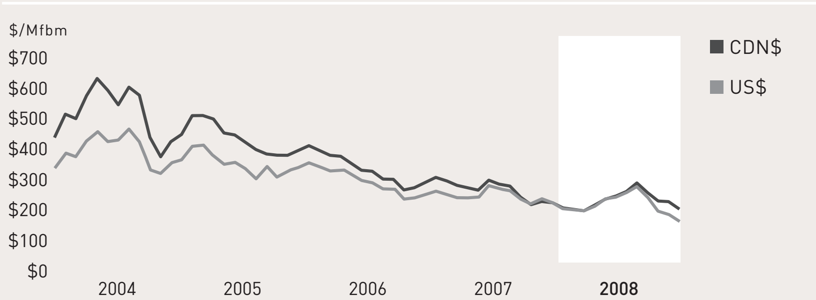

### ii. CONTINUED STRONG CANADIAN DOLLAR AND EXPORT TAX

The majority of Canfor's sales are denominated in US dollars, and Canfor's results are therefore impacted by movements in the exchange rate. The average value of the Canadian dollar in 2008 was up marginally (0.8 cents, or 1%) versus its U.S. counterpart compared to 2007. The Canadian dollar remained around par with the U.S. dollar for most of the year; as the global economy worsened, however, it weakened considerably in the final quarter of 2008 ending the year at $0.817, some 19.5 cents, or 19.3%, lower than at the end of 2007.

(1) U.S. Bureau of the Census
(2) NAR – National Association of Realtors
(3) Random Lengths

The following chart depicts the trend in monthly average benchmark Western SPF 2x4 #2&Btr lumber prices, with the Canadian dollar prices representing the US dollar price multiplied by the monthly average exchange rate:

U.S. AND CANADIAN WESTERN SPF 2X4 #2 RL LUMBER PRICE COMPARISON




Except for Canfor's Daaquam operation, which, as a border mill, benefits from tax-exempt status under the Softwood Lumber Agreement ("SLA"), and a Third Country Adjustment export tax refund for the last quarter of 2007 and first quarter of 2008, Canfor's lumber exports to the U.S. have been subject to the highest export tax bracket of 15% since the SLA came into effect in October of 2006. The Company has paid export taxes of approximately $188 million from October of 2006 to December of 2008.

## SIGNIFICANT CURTAILMENTS AND CLOSURES

As a result of continued weak demand and low pricing for softwood lumber, OSB and plywood, the Company reduced its production volume significantly in 2008. The downtime took the form of indefinite idling for several operations in the B.C. Interior, and shortened workweeks or reduced shifts at its other operations in B.C., Quebec and the U.S. south-east.

The Company curtailed approximately one quarter of its lumber capacity, and the significant majority of its panels capacity, in 2008. Canfor is not currently producing any plywood and the only panels business currently operating is the jointly owned Peace Valley ("PV") OSB mill in Fort St. John, B.C.

A summary of the lumber and panel operations idled in 2008, and the reduction in annual production capacity is presented below:

LUMBER

- Chetwynd (British Columbia) – Indefinite closure in March of 2008, reducing annual SPF lumber capacity by approximately 219 million board feet.
- Mackenzie (British Columbia) – Indefinite closure in June of 2008, reducing annual SPF lumber capacity by approximately 305 million board feet.

PANELS

- PolarBoard (Fort Nelson, British Columbia) – Indefinite closure in June of 2008, reducing annual OSB capacity by approximately 640 million square feet (3/8" basis).
- Tackama (Fort Nelson, British Columbia) – Indefinite closure in October of 2008, reducing annual plywood capacity by approximately 270 million square feet (3/8" basis).

In May of 2008, a fire at Canfor's NCP facility located in Prince George, B.C. destroyed the facility. The Company subsequently decided not to rebuild the plant, but expects to reinvest the insurance proceeds in its existing facilities to improve the cost competitiveness of its operations. NCP had an annual production capacity of plywood of 170 million square feet prior to the fire.

## IMPROVED OPERATIONAL PERFORMANCE AND TIGHT COST CONTROL

The Company recorded a much improved operational performance in 2008. The lumber business segment, in particular, saw significant cost reductions and performance improvements, as evidenced by a 14% decrease in year-over-year unit manufacturing costs at the B.C. Interior operations. This improvement was achieved in the face of an additional 700 million board feet of curtailment. Rising losses in the panels business segment were mitigated with the indefinite closures of the PolarBoard and Tackama operations. Canfor Pulp Limited Partnership ("CPLP") and Taylor Pulp recorded solid operational performances in 2008, but the slump in market demand and prices late in the year significantly eroded earnings.

Working capital and capital spending continued to be closely managed in 2008. Capital spending was restricted to essential maintenance-of-business expenditures and selected high-return projects. The latter included the commencement of a new energy system at the Company's Fort St. John facility, and the completion of key capital upgrades at the Company's Conway mill in South Carolina. The more significant pulp capital expenditures related to various upgrades at CPLP's Intercon and Northwood pulp mills and the replacement of a chip screening and in-feed system at CPLP's Prince George Pulp and Paper ("PG Pulp") mill. The latter was required as a result of a fire in early 2008 and was mostly funded by insurance proceeds.

The Company ended the year with cash on hand of $362.4 million, as well as unused available operating lines of credit of $363.4 million, and a net debt to total capitalization ratio of 15%.

## OVERVIEW OF CONSOLIDATED RESULTS – 2008 COMPARED TO 2007

### SELECTED FINANCIAL INFORMATION AND STATISTICS:

| (millions of dollars, except for per share amounts) | 2008 | 2007 |
|---|---|---|
| Sales | $ 2,611.6 | $ 3,275.6 |
| EBITDA[4] | $ 13.1 | $ (88.9) |
| Operating loss[4] | $ (158.1) | $ (273.0) |
| Foreign exchange (loss) gain on long-term debt and investments, net | $ (100.3) | $ 16.2 |
| (Loss) gain on derivative financial instruments[5] | $ (88.5) | $ 16.0 |
| Asset impairments | $ (169.6) | $ (268.0) |
| Prince George Pulp & Paper mill fire, net | $ 8.2 | $ – |
| North Central Plywoods mill fire, net | $ 57.9 | $ – |
| Net loss[4] | $ (345.2) | $ (360.6) |
| Net loss per share, basic and diluted[4] | $ (2.42) | $ (2.53) |
| Average exchange rate (US$/CDN$)[6] | $ 0.938 | $ 0.930 |
| U.S. housing starts (million units SAAR)[7] | 0.902 | 1.341 |

(4) Results for 2008 reflect the Company's retrospective adoption (without prior period restatement) on January 1, 2008 of CICA Handbook Section 3031, Inventories, which requires all inventories, including logs, to be valued at the lower of cost or net realizable value. Details of related write-downs and reversals are contained in the following pages. The adjustments affect comparability with prior periods.
(5) Includes gains (losses) from natural gas, diesel, foreign exchange and lumber price derivatives (see "Non-Segmented Items" section for more details).
(6) Source – Bank of Canada (average noon rate for the period)
(7) Source – U.S. Census Bureau, seasonally adjusted annual rate ("SAAR")

### ANALYSIS OF SPECIFIC ITEMS AFFECTING COMPARABILITY OF NET LOSS

| After-tax impact, net of non-controlling interests (millions of dollars, except for per share amounts) | 2008 | 2007 |
|---|---|---|
| **Net loss as reported** | $ (345.2) | $ (360.6) |
| Loss (gain) on derivative financial instruments | $ 54.5 | $ (11.6) |
| New inventory accounting standard | $ (18.7) | $ – |
| Foreign exchange loss (gain) on long-term debt and investments, net | $ 72.2 | $ (6.5) |
| Prince George Pulp & Paper mill fire, net | $ (3.4) | $ – |
| North Central Plywoods mill fire, net | $ (45.0) | $ – |
| Restructuring, mill closure and severance costs | $ 35.3 | $ 27.3 |
| Corporate income tax rate reductions | $ (9.1) | $ (37.7) |
| Asset impairments | $ 131.0 | $ 199.2 |
| Other items | $ 0.1 | $ (9.1) |
| Net impact of above items | $ 216.9 | $ 161.6 |
| **Net loss, as adjusted** | $ (128.3) | $ (199.0) |
| **Net loss per share, as reported** | $ (2.42) | $ (2.53) |
| Net impact of above items per share | $ 1.52 | $ 1.13 |
| **Net loss per share, as adjusted** | $ (0.90) | $ (1.40) |

## EBITDA

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

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| **Net loss as reported** | $ (345.2) | $ (360.6) |
| Add (subtract): | | |
| Non-controlling interests | $ 24.0 | $ 65.4 |
| Income tax recovery | $ (141.9) | $ (234.1) |
| Other (income) expense | $ (12.7) | $ 11.1 |
| Loss (gain) on derivative financial instruments | $ 88.5 | $ (16.0) |
| Asset impairments | $ 169.6 | $ 268.0 |
| Foreign exchange loss (gain) on long-term debt and investments, net | $ 100.3 | $ (16.2) |
| Prince George Pulp & Paper mill fire, net | $ (8.2) | $ – |
| North Central Plywoods mill fire, net | $ (57.9) | $ – |
| Interest expense, net | $ 25.4 | $ 9.4 |
| Amortization | $ 171.2 | $ 184.1 |
| **EBITDA, as reported** | $ 13.1 | $ (88.9) |
| Restructuring, mill closure and severance costs | $ 53.5 | $ 41.3 |
| **Adjusted EBITDA** | $ 66.6 | $ (47.6) |
| Log inventory recovery resulting from new inventory accounting standard, included in EBITDA | $ 30.4 | $ – |

The Company recorded a net loss of $345.2 million ($2.42 per share) for the year ended December 31, 2008, $15.4 million less than the net loss of $360.6 million ($2.53 per share) reported for the year ended December 31, 2007.

After adjusting for significant items affecting comparability with prior periods, the Company's adjusted net loss was $128.3 million ($0.90 per share) for 2008, compared to a similarly adjusted net loss of $199.0 million ($1.40 per share) for 2007.

The Company recorded an operating loss of $158.1 million in 2008, an improvement of $114.9 million compared to 2007. Reported EBITDA was $13.1 million, an improvement of $102.0 million from the previous year. For the most part, the positive variances reflected significantly reduced operating losses for the Company's lumber business which more than offset lower earnings in the pulp and paper business.

For the lumber business, the positive impact of substantially reduced log and conversion costs and, to a lesser extent, a Third Country Adjustment export tax refund and increased residual fibre realizations, more than outweighed lower prices and the slightly higher average Canadian dollar. The Panels business also recorded lower losses in 2008, with the mitigation of losses through curtailments and lower log costs more than offsetting higher restructuring, mill closure and severance costs. Average OSB prices in 2008 showed a modest increase, while plywood prices were down 10%. Corporate costs continued to trend downwards in 2008.

The lower pulp and paper earnings reflected higher fibre, energy, chemical and maintenance costs and a slowing order file in the last quarter of 2008; Canadian dollar pulp price realizations were down slightly year-over-year, as higher freight costs, a lower-value geographical mix and a stronger Canadian dollar (particularly for the first nine months of 2008) more than offset higher average NBSK pulp list and BCTMP prices in 2008.

The 2008 operating results also reflected the Company's adoption of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3031, Inventories, on January 1, 2008, which requires inventories, including logs, to be valued at the lower of cost or net realizable value (previously, the Company valued logs at the higher of net realizable value and replacement cost, if lower than average cost). The adoption of the new accounting standard resulted in an increase in 2008's operating income and net income by $30.4 million and $18.7 million ($0.13 per share), respectively, due principally to a combination of a significant reduction in log costs and volumes through 2008.

A more detailed review of the Company's operational performance and results is provided in "Operating Results by Business Segment – 2008 compared to 2007", which follows this overview of consolidated results.

Reflecting a significant erosion of the value of the Canadian dollar in the last quarter of 2008, the Company recorded a foreign exchange translation loss on its US dollar denominated debt less investments of $100.3 million (2007 – gain of $16.2 million). The weaker Canadian dollar was also a significant contributor to 2008 losses recorded on derivative financial instruments of $88.5 million (2007 – gain of $16.0 million); the significant majority of the losses reflected mark-to-market losses at year end on unrealized forward exchange collars and forward contracts and energy swaps and options.

As a result of the very challenging operating climate and market outlook, the Company recorded asset impairment charges totalling $169.6 million in 2008 (2007 – $268.0 million). The charges comprised the following:

- $89.4 million related to the solid wood business in 2008, principally on the Company's PolarBoard and Tackama indefinitely idled panel assets.
- $70.0 million related to balances owing from Howe Sound Pulp and Paper Limited Partnership ("HSLP") and the Company's investment in Coastal Fibre Limited Partnership ("CFLP"), reflecting weaker B.C. Coastal pulp, paper and fibre market conditions.
- $10.2 million related to the Company's investment in non-bank asset-backed commercial paper ("ABCP").

In connection with the fire at the Company's NCP facility that destroyed the mill, the Company recorded a pre-tax gain of $57.9 million, based on preliminary estimates of net property damage insurance proceeds receivable and costs related to the fire. The insurance property damage receivable was estimated on the basis that the insurance proceeds will be applied towards capital improvements at Canfor's other operations.

## OPERATING RESULTS BY BUSINESS SEGMENT – 2008 COMPARED TO 2007

The following discussion of Canfor's operating results relates to the operating segments and the non-segmented items as per the Segmented Information note in the Company's consolidated financial statements.

Canfor's operations include the following three operating segments: Lumber, Panels and Pulp and Paper.

### LUMBER

The Lumber segment consists of logging and forestry operations, which manage approximately 11.3 million cubic metres of allowable annual cut in British Columbia, northern Alberta and Quebec, and own 13 sawmills in British Columbia, one in Alberta, one in Quebec, three in South Carolina and one in North Carolina. The combined lumber production capacity of these sawmills is approximately 4.9 billion board feet. Other operations include two lumber remanufacturing facilities, one in British Columbia and one in Washington State, a whole-log chipping plant and a finger-joint mill. The South Carolina operations include two lumber treating plants, a finger joint plant, and a trucking division. The segment also includes Canfor's wood products marketing division, located in Vancouver. Also included is Canfor's 60% interest in the Houston Pellet Plant, which has an annual capacity of 150,000 tonnes of wood pellets. Canfor markets lumber products throughout North America as well as overseas. In addition to its own products, Canfor also markets lumber products from independent mills and offshore suppliers to complement its product line.

Under the SLA, implemented by the federal governments of Canada and the United States on October 12, 2006, Canadian softwood lumber exporters pay an export tax on lumber shipped to the U.S. when the price of lumber is at or below US$355 per Mfbm, as determined by the Random Lengths Framing Lumber Composite Price ("RLCP"). The export tax rate is determined monthly, with the rate being based on the following trigger prices:

| Trigger RLCP Price | Tax Rate |
|---|---|
| Over US$355 | 0% |
| US$336–$355 | 5% |
| US$316–$335 | 10% |
| US$315 and under | 15% |

The SLA also includes a "Surge Mechanism", which increases the export tax rate for the month by 50% when the monthly volume of exports from a region exceeds a "Trigger Volume" as defined in the SLA.

In December of 2008, the Company received information from the Canada Revenue Agency indicating it was eligible to claim a Third Country Adjustment refund under the SLA of a third of the 15% export charges paid for the quarters ended December 31, 2007 and March 31, 2008. The claim is based on year-over-year movements in the Canadian and U.S. market share of total U.S. consumption of softwood lumber products and the share of U.S. consumption from imports not originating in Canada. The Company has filed for a refund of $10.8 million for those periods.

## SELECTED FINANCIAL INFORMATION AND STATISTICS – LUMBER

Summarized results for the Lumber segment for 2008 and 2007 are as follows:

| (millions of dollars, unless otherwise noted) | 2008 | 2007 |
|---|---|---|
| Sales | $ 1,490.5 | $ 1,942.7 |
| EBITDA[8] | $ (55.5) | $ (198.4) |
| Adjusted EBITDA | $ (36.8) | $ (176.7) |
| EBITDA margin[8] | (4)% | (10)% |
| Adjusted EBITDA margin | (2)% | (9)% |
| Operating loss[8] | $ (155.0) | $ (301.2) |
| Capital expenditures | $ 39.5 | $ 47.6 |
| Average SPF 2x4 #2 & Btr lumber price in US$[9] | $ 222 | $ 250 |
| Average SPF price in Cdn$ | $ 237 | $ 269 |
| Average SYP 2x4 #2 lumber price in US$[10] | $ 281 | $ 280 |
| Average SYP price in Cdn$ | $ 300 | $ 301 |
| Production – SPF lumber (MMfbm) | 3,299.4 | 4,111.6 |
| Production – SYP lumber (MMfbm) | 388.6 | 389.2 |
| Shipments – Canfor-produced SPF lumber (MMfbm)[11] | 3,388.2 | 4,233.5 |
| Shipments – Canfor-produced SYP lumber (MMfbm)[11] | 432.7 | 448.7 |
| Shipments – wholesale lumber (MMfbm) | 171.0 | 325.2 |

(8) EBITDA and Operating loss for the year ended December 31, 2008 include income of $17.3 million related to the implementation of new log inventory accounting. The income resulted principally from reversal of previously recognized log inventory write-downs at the beginning of the year (recorded through opening retained earnings), as lower log and conversion costs and the weaker Canadian dollar combined to more than offset the impact of lower finished product prices.
(9) Western Spruce/Pine/Fir, per thousand board feet (Source – Random Lengths Publications, Inc.)
(10) Southern Yellow Pine, Eastside, per thousand board feet (Source – Random Lengths Publications, Inc.)
(11) Includes shipments of lumber purchased for remanufacture.

### OVERVIEW

The Lumber segment reported an operating loss of $155.0 million for 2008, an improvement of $146.2 million compared to 2007. Reported EBITDA and Adjusted EBITDA improved $142.9 million and $139.9 million, respectively. Total market-related curtailment in 2008 was approximately 1.2 billion board feet, up 700 million board feet from 2007.

The increase in EBITDA and Adjusted EBITDA reflected significantly reduced unit manufacturing costs and losses mitigated through curtailment, which more than offset weaker prices for both SPF 2x4 and wider SPF and SYP grades. Other contributing factors to the improved performance included higher residual fibre realizations and the Third Country Adjustment export tax refund, which were partly offset by the negative impact on sales realizations of a 1% increase in the average value of the Canadian dollar. Restructuring costs were $18.7 million in 2008, down $3.0 million from the previous year.

### MARKETS

Canfor's total lumber sales volume for 2008 was 3,992 million board feet, down 20% from 2007, with SPF sales and SYP sales making up 89% and 11% of sales, respectively.

In 2008, sales to the U.S. accounted for 72% of total sales revenue, down 3% from 2007, as the Company increased its proportion of sales to Canada and the Far East. A breakdown of lumber sales by country for 2008 and 2007 is provided below:

**Lumber Sales by Country (based on dollar values):**

| | 2008 | 2007 |
|---|---|---|
| U.S. | 72% | 75% |
| Canada | 16% | 15% |
| Far East | 11% | 9% |
| Other | 1% | 1% |
| | 100% | 100% |

Lumber markets continued to erode in 2008 as U.S. housing starts plunged to the lowest level on record by the end of the year. Total U.S. housing starts were 902,000 units in 2008[12], a 33% decrease from 1.341 million units in 2007. Starts declined significantly through 2008, ending the year at 550,000 units (SAAR) in December, the lowest level since records began in 1959. Inventories of new and used homes available for sale in the U.S. market at the end of 2008 were 12.9 months and 9.3 months[13], respectively, well above historical levels.

The Canadian housing market remained fairly stable for most of 2008, before tapering off towards the end of the year. Total Canadian housing starts were 211,000 units[14], a decrease of 8% from the 2007 total of 228,300 units.

Repair and Remodeling sales in the U.S. also declined in 2008 compared to the previous year, albeit at a slower pace than new home sales. The Company's sales to Home Centre customers as a proportion of sales in 2008 were in line with 2007.

The SPF lumber 2x4 #2&Btr price reached a short-lived high of US$283 per Mfbm[15] in August of 2008, before declining rapidly through the balance of the year. Average prices across all SPF and SYP grades were down compared to the prior year, except for SYP 2x4 #2&Btr, where the yearly average price was largely unchanged.

Total Japanese housing starts for 2008 were 1.1 million, an increase of 3% over 2007[16] with western style 2x4 housing starts up 9% over the same period. As a result of a highly competitive market place, Canfor's sales to Japan for 2008 decreased from 2007, but in contrast sales to China in 2008 showed a 30% increase compared to 2007.

### SALES

Lumber sales revenues for 2008 were down $452.2 million, or 23%, compared to 2007, reflecting the 20% decline in shipments and price erosion across almost all grades in 2008. 2008 shipments were down 1,016 million board feet compared to 2007, as the Company responded to weaker demand with significantly increased production curtailment. The average price for SPF benchmark 2x4 #2&Btr was down US$28 per Mfbm, or 11%, compared to the prior year, while average prices for SYP lumber, measured by 2x4 #2&Btr, were almost unchanged. More significantly, however, prices for wider SPF and SYP grades fell sharply in 2008, as evidenced by year-over-year SPF and SYP 2x10 price declines of 22% and 16%, respectively. The 1% decrease in the US dollar versus the Canadian dollar also contributed to lower Canadian dollar sales realizations in 2008.

Total residual fibre revenue for 2008 was well down from 2007 levels, reflecting significantly lower sawmill operating rates, but the average unit chip prices showed a modest increase in 2008, primarily as a result of higher average NBSK pulp prices.

### OPERATIONS

Lumber production for 2008 was 3,688 million board feet, 813 million board feet, or 18%, lower than for 2007. This lower production reflected the indefinite closures of the Mackenzie (June) and Chetwynd (March) sawmills, as well as a combination of reduced shifts and shortened work weeks at the Company's other operations. Production in 2008 included the Darlington sawmill in South Carolina, which was acquired in late 2007.

Despite the challenges presented by curtailments to its operations, the Company made significant headway in reducing its controllable costs in 2008. Total unit manufacturing costs were down at the majority of the Company's operations, and at its B.C. Interior operations unit costs were down 14% compared to the prior year. Major contributing factors to the improved cost performance were reduced unit log costs, achieved through reduced operating and overhead costs, and lower unit conversion costs that for the most part reflected improved sawmill and planer productivity and reduced overhead costs.

The Company's export tax expense in 2008 was $55.1 million (2007 – $101.8 million). While the export tax on shipments remained at 15% through 2008, lower shipments to the U.S. in 2008 and the Third Country Adjustment refund resulted in the lower expense compared to 2007.

(12) U.S. Bureau of the Census
(13) NAR – National Association of Realtors
(14) CMHC
(15) Random Lengths
(16) Japanese Ministry of Land, Infrastructure, Transport and Tourism

## PANELS

The Panels segment includes the Tackama plywood plant, with an annual production capacity of 270 million square feet (3/8" basis), and the PolarBoard OSB facility, with an annual production capacity of 640 million square feet (3/8" basis), both of which are currently indefinitely closed. Also included in this segment is the Peace Valley OSB ("PV OSB") mill, which is jointly owned with Louisiana Pacific Corporation, of which Canfor's share is 50%. The PV OSB mill has an annual capacity of 820 million square feet (3/8" basis). Prior to the NCP fire in May of 2008 the Panels segment also included this mill's annual plywood production capacity of 170 million square feet. This capacity has now been permanently removed following the Company's decision not to rebuild the facility.

The OSB that Canfor produces is largely performance rated sheathing and flooring, used in wall, roof and flooring construction of new homes and in Repair and Remodeling projects. Canfor's plywood is primarily sheathing, used to frame walls in new homes. The majority of Canfor's OSB sales are to the U.S. market. Canada is the largest market for Canfor's plywood. Substantially all panel products destined for North American markets were shipped either by rail or truck.

### SELECTED FINANCIAL INFORMATION AND STATISTICS – PANELS

| (millions of dollars, unless otherwise noted) | 2008 | 2007 |
|---|---|---|
| Sales | $ 170.3 | $ 297.7 |
| EBITDA[17] | $ (40.8) | $ (53.5) |
| Adjusted EBITDA | $ (6.3) | $ (39.0) |
| EBITDA margin[17] | (24)% | (18)% |
| Adjusted EBITDA margin | (4)% | (13)% |
| Operating loss[17] | $ (56.9) | $ (76.5) |
| Capital expenditures | $ 0.8 | $ 15.7 |
| Average plywood price in Cdn$[18] | $ 338 | $ 376 |
| Average OSB in US$[19] | $ 172 | $ 161 |
| Average OSB price in Cdn$ | $ 183 | $ 173 |
| Production – plywood (MMsf 3/8") | 233.4 | 385.0 |
| Production – OSB (MMsf 3/8") | 434.8 | 673.2 |
| Shipments – plywood (MMsf 3/8") | 264.1 | 385.4 |
| Shipments – OSB (MMsf 3/8") | 462.9 | 669.9 |

(17) EBITDA and Operating loss for the year ended December 31, 2008 include income of $13.1 million related to the implementation of new log inventory accounting. The majority of income resulted from the consumption in 2008 of December 31, 2007 log inventory volumes (on which write-downs to net realizable value were recorded through opening retained earnings) and significantly reduced log inventory volumes at the end of 2008.

(18) Canadian softwood plywood, per Msf 3/8" basis, delivered to Toronto (Source – C.C. Crowe Publications, Inc.)

(19) OSB, per Msf 7/16" North Central (Source – Random Lengths Publications, Inc.)

#### OVERVIEW

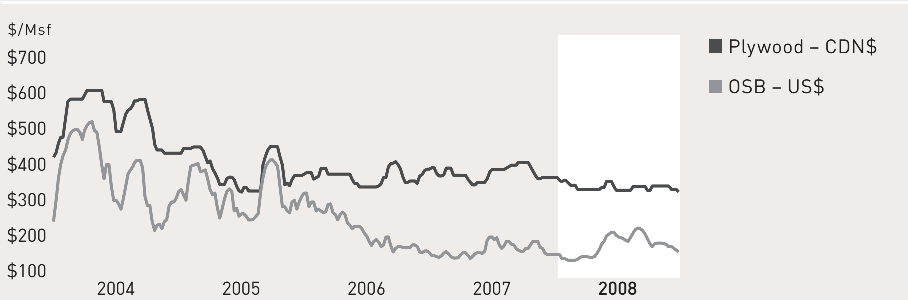
The Panels segment recorded an operating loss of $56.9 million for 2008, $19.6 million less than the operating loss reported for 2007.

The 2008 and 2007 operating losses included restructuring, mill closure and severance costs of $34.5 million and $14.4 million, respectively. Costs for 2008 reflected the indefinite closures of PolarBoard (June) and Tackama (October), as well as the permanent closure of NCP following the May fire that destroyed the facility. The 2007 costs reflected the permanent closure of the Company's Panel & Fibre operation in December of 2007. Adjusted EBITDA for 2008 was up $32.8 million compared to 2007, and reflected reduced losses arising from the Company's decision to curtail most of its production, the impact of the new log inventory accounting standard in 2008, and lower log costs.

MARKETS

The North American structural panel market in 2008 was affected by the same factors as the lumber market, with the substantial reduction in U.S. housing starts placing significant downward pressure on panel prices throughout the year. The 2008 price of OSB averaged US$172 per thousand square feet ("Msf"), 7/16" North Central[20] an increase of 7% above 2007 average price of US$161 per Msf, although prices fell off sharply later in the year, ending 2008 at US$153 per Msf. Canadian plywood prices averaged $338 per Msf, a decrease of 10% from 2007 for Canadian softwood plywood delivered to Toronto. Prices ended the year at $323 per Msf.

PANEL PRICE HISTORY




SALES

OSB Canadian dollar sales realizations were up slightly for 2008 compared to 2007. Modest increases in OSB prices outweighed the slightly stronger Canadian dollar, but were offset by the lower plywood prices in 2008. Total shipment volumes were down 328 million square feet, or 31%, reflecting the NCP mill permanent closure in 2008, the indefinite closures of PolarBoard and Tackama, and also, to a lesser extent, curtailment at the PV OSB mill in the final quarter of 2008.

OPERATIONS

Production volumes in 2008 were down 390 million feet, or 37%, in 2008 compared to 2007, as a result of the significantly reduced operating rates. Total unit manufacturing costs showed a modest improvement in 2008, mostly due to lower log costs and higher press productivity, which more than offset higher unit overhead costs linked to the large declines in production.

## PULP AND PAPER

Canfor's Pulp and Paper segment is comprised of Canfor Pulp Limited Partnership ("CPLP") and the Taylor Pulp mill ("Taylor"). CPLP produces northern bleached softwood kraft ("NBSK") pulp and specialty paper. NBSK pulp is primarily a bleached product, although unbleached and semi-bleached grades are also produced at the PG Pulp mill. All of the operations are located within five kilometres of each other in Prince George, British Columbia with the exception of Taylor, which is located near Fort St. John, British Columbia.

The CPLP pulp mills have the capacity to produce over one million tonnes of NBSK pulp annually. Over 200,000 tonnes of bleached chemi-thermo mechanical pulp ("BCTMP") per year can be produced at the Taylor mill. The paper machine, located at the PG Pulp mill, has an annual capacity, at optimum product mix levels, to produce 140 thousand tonnes of kraft paper.

CPLP's pulp marketing division is located in Vancouver. All pulp produced by CPLP, Taylor and the Howe Sound Limited Partnership (discussed under "Related Party Transactions") is sold by CPLP's sales and marketing group to customers primarily in North America, Europe and Asia. The kraft paper produced by CPLP is sold by a 50% owned general partnership to customers in North America and Europe.

(20) Random Lengths

## SELECTED FINANCIAL INFORMATION AND STATISTICS – PULP AND PAPER[21]

| (millions of dollars, unless otherwise noted) | 2008 | 2007 |
|---|---|---|
| Sales | $ 950.8 | $ 1,035.2 |
| EBITDA | $ 125.6 | $ 190.5 |
| EBITDA margin | 13% | 18% |
| Operating income | $ 76.8 | $ 137.2 |
| Capital expenditures | $ 39.9 | $ 24.2 |
| Average pulp price delivered to U.S. – in US$[22] | $ 857 | $ 823 |
| Average pulp price in Cdn$ | $ 914 | $ 885 |
| Production – pulp (000 mt) | 1,124.6 | 1,244.5 |
| Production – paper (000 mt) | 132.6 | 131.6 |
| Shipments – Canfor-produced pulp (000 mt) | 1,088.0 | 1,228.9 |
| Pulp marketed on behalf of HSLP (000 mt)[23] | 313.1 | 366.6 |
| Shipments – paper (000 mt) | 124.8 | 129.5 |

(21) Includes Taylor and 100% of CPLP, which is consolidated in Canfor's operating results. Pulp production and shipment volumes presented are for both NBSK pulp and BCTMP.
(22) Per tonne, NBSK pulp list price delivered to U.S. (RISI)
(23) Howe Sound Pulp and Paper Limited Partnership Pulp mill

### OVERVIEW

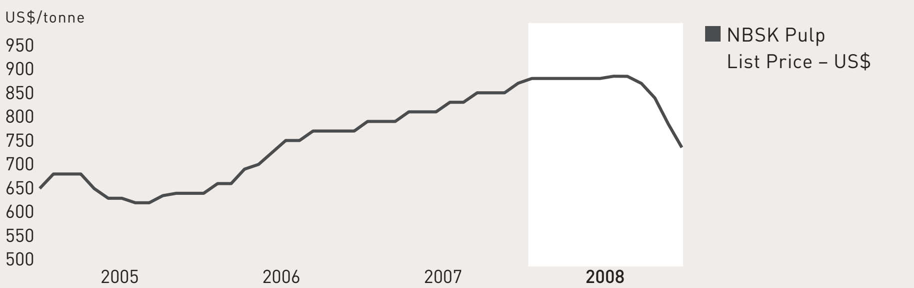
Operating income and EBITDA in the Pulp and Paper segment for 2008 were down $60.4 million and $64.9 million, respectively, from the prior year. The unfavourable variances were primarily attributable to higher fibre, energy, chemical and freight costs, higher scheduled maintenance outages, and the rapid deterioration of market conditions later in the year which resulted in market downtime in the fourth quarter. Overall realized pulp prices in Canadian dollar terms were largely unchanged in 2008, as higher BCTMP transaction prices helped to offset slight decreases in both the value of the U.S. dollar and realized NBSK pulp prices, where a higher percentage of spot sales into Asia at lower than published list prices, particularly in the later part of the year, offset higher average list prices.

### MARKETS

After a strong start to 2008, pulp market conditions started to weaken during the third quarter before plummeting in the final quarter of the year as the financial and credit market crisis and worsening global economic conditions took their toll. At the end of the year, market pulp inventories of softwood kraft market pulp were at 40 days of supply[24] which represented an increase of 13 days compared to the end of 2007. Inventories of 30 days are generally considered to be representative of a balanced market. The Pulp and Paper Products Council ("PPPC") reported total Global 100 chemical market pulp shipments at a rate of 87% in 2008, compared to 92% for 2007.

While the average NBSK pulp list price delivered to the U.S. was US$857 per tonne, up about 4% from 2007, list prices at year end were US$730 per tonne, US$150 per tonne, or 17%, lower than twelve months earlier. Price erosion was even more significant in European markets, where list prices fell US$245 per tonne over the same period, and also in Asia where spot sales prices fell off sharply, particularly in the latter part of 2008. The following chart highlights the significant downward trend in NBSK Pulp List Price delivered to the U.S in the second half of 2008:

NBSK PULP LIST PRICE DELIVERED TO U.S.




(24) Pulp and Paper Products Council ("PPPC")

SALES

Shipments of Canfor-produced pulp were down 11% compared to the prior year. Sales volumes were down 199,000 tonnes when compared to the prior year due to a combination of a fire that destroyed CPLP's PG Pulp mill's chip screening and in-feed system in the first quarter, increased scheduled maintenance outages and market related downtime in 2008, the latter precipitated by the reduction in global paper demand later in the year. Realized pulp prices in Canadian dollar terms were largely unchanged in 2008, as higher prices, particularly for BCTMP products, offset a 1% strengthening of the Canadian dollar and weaker NBSK pulp prices, particularly in the second half of 2008, which reflected a higher proportion of spot sales to Asian markets and significantly slower demand. Specialty paper prices showed a moderate improvement over 2007. Freight costs on shipments of finished product were also up significantly in 2008.

OPERATIONS

Production volume for 2008 was down 119,000 tonnes, or 9%, when compared to the prior year, mainly due to a fire at PG Pulp mill's chip screening and in-feed system in the first quarter of 2008, higher scheduled maintenance downtime and NBSK and BCTMP market curtailment taken late in the year. Higher unit manufacturing costs reflected reduced operating rates and higher scheduled maintenance costs as well as increased energy, chemical and fibre costs. The increase in fibre costs in part resulted from a higher proportion of whole log chipping due to a significant reduction in sawmill residual chips due to poor lumber markets, as well as higher in-bound freight costs. Higher chemical and energy costs were attributable to commodity price inflation. Offsetting the impact of the PG Pulp mill's fire were business interruption insurance recoveries of $19.1 million.

## NON-SEGMENTED ITEMS

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Corporate and other costs | $ (23.0) | $ (32.5) |
| Interest expense, net | $ (25.4) | $ (9.4) |
| Foreign exchange (loss) gain on long-term debt and investments, net | $ (100.3) | $ 16.2 |
| (Loss) gain on derivative financial instruments | $ (88.5) | $ 16.0 |
| Asset impairments | $ (169.6) | $ (268.0) |
| Prince George Pulp & Paper mill fire, net | $ 8.2 | $ – |
| North Central Plywoods mill fire, net | $ 57.9 | $ – |
| Other income (expense), net | $ 12.7 | $ (11.1) |

### CORPORATE AND OTHER COSTS

Corporate and other costs, which comprise corporate, head office and certain information technology costs, decreased by $9.5 million in 2008 compared to 2007, due primarily to reduced staffing and other cost reduction initiatives, as well as costs associated with the resignation of the Company's former chief executive officer recorded in 2007.

### INTEREST INCOME AND EXPENSE

Net interest expense for the third quarter was $25.4 million, up $16.0 million compared to 2007. The increase primarily related to higher average net indebtedness in 2008.

### FOREIGN EXCHANGE GAIN (LOSS) ON TRANSLATION OF LONG-TERM DEBT AND INVESTMENTS

As a result of a 24% appreciation of the US dollar (relative to the Canadian dollar) through 2008, most of which occurred in the last quarter of the year, the Company recorded a foreign exchange translation loss on its US dollar denominated debt less investments of $100.3 million, in contrast to a gain of $16.2 million recorded in 2007.

## GAIN (LOSS) ON DERIVATIVE FINANCIAL INSTRUMENTS

The Company uses a variety of derivative financial instruments as partial economic hedges against unfavourable changes in natural gas and diesel costs, foreign exchange rates and lumber prices. In 2008, the Company recorded a loss of $88.5 million related to its derivative instruments, which reflected a sharp decline in the value of the Canadian dollar and energy prices in the last part of the year. The following table summarizes the amounts of the various components for the comparable periods.

**Gain (Loss) on Derivative Financial Instruments:**

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Foreign exchange collars and forward contracts | $ (86.1) | $ 14.3 |
| Natural gas swaps | $ 1.0 | $ (9.1) |
| Diesel options and swaps | $ (3.4) | $ 9.1 |
| Commodity futures | $ – | $ 1.7 |
| | $ (88.5) | $ 16.0 |

## ASSET IMPAIRMENTS

The Company recorded asset impairment charges totalling $169.6 million in 2008 (2007 – $268.0 million), which consisted of the following:

- $89.4 million related to the downturn in the solid wood business in 2008, principally related to the Company's Tackama and PolarBoard operations, both of which were indefinitely idled during the year.
- $70.0 million related to balances owing from HSLP and the Company's 50% interest in CFLP, an entity which supplies fibre and related services to HSLP. The impairment reflected the continuing deterioration of B.C. Coastal pulp, paper and fibre market conditions.
- $10.2 million related to the Company's investment in ABCP. This resulted from the estimated fair value of the ABCP at year end, which took into account all information available to Canfor related to its specific holdings of ABCP. It also assumed a high likelihood of success for an ABCP restructuring plan which was approved by regulators in 2008. The restructuring plan was subsequently completed on January 21, 2009.

More information on the asset impairments is contained under "Critical Accounting Estimates – Asset Impairments".

## PRINCE GEORGE PULP AND PAPER MILL FIRE

A gain of $8.2 million was recorded by CPLP in 2008, arising from the fire that destroyed a chip screening and in-feed system at its PG Pulp mill in the first quarter.

## NCP MILL FIRE

In May of 2008, a fire at the Company's NCP facility completely destroyed the mill. The mill was insured for equivalent replacement value. At the end of 2008, the Company had not reached a final settlement with its insurer, and accordingly, estimated the insurance property damage amount receivable using preliminary engineering estimates and other information available. Based on estimated insurance proceeds, net of an aggregate policy deductible of $2.4 million, and costs related to the fire, the Company recorded a pre-tax gain of $57.9 million. The estimates are subject to adjustments in future periods. The Company received cash advances of $30.0 million from its insurer by the end of 2008. The insurance property damage receivable was estimated on the basis that the insurance proceeds will be applied towards capital improvements at Canfor's other operations.

## OTHER INCOME AND EXPENSE

Other income amounted to $12.7 million in 2008, compared to an expense of $11.1 million in 2007. In both years, the significant majority of these amounts reflected foreign exchange movements on US dollar denominated cash, receivables and payables of Canadian operations.

### INCOME TAX RECOVERY

The Company recorded an income tax recovery of $141.9 million in 2008, compared to a recovery of $234.1 million in 2007.

The 2008 recovery is comprised of a current income tax recovery of $47.9 million and a future income tax recovery of $94.0 million. The most significant factors contributing to the future income tax recovery are the impact of the asset impairment charge, which gave rise to a recovery of $36.7 million, the impact of the loss on the derivative financial instruments, which gave rise to a recovery of $28.4 million, and the impact of the unrealized foreign exchange losses on translation of long-term debt and investments, which gave rise to a recovery of $13.5 million.

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

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Net loss before income taxes and non-controlling interests | $ (463.1) | $ (529.3) |
| Income tax recovery at statutory rate | 143.6 | 180.5 |
| Add (deduct): | | |
| Non-controlling interests | 7.4 | 22.3 |
| Change in corporate income tax rates | 9.1 | 21.5 |
| Entities with different income tax rates and other tax adjustments | 4.4 | 12.4 |
| Tax recovery at rates other than statutory rate | 3.5 | – |
| Permanent difference from capital gains and losses and other non-deductible items | (26.1) | (2.6) |
| Income tax recovery | $ 141.9 | $ 234.1 |

## SUMMARY OF FINANCIAL POSITION

The following table summarizes Canfor's financial position as at the end of the years 2008 and 2007:

| (millions of dollars, except for ratios) | 2008 | 2007 |
|---|---|---|
| Net cash | $ 362.4 | $ 295.5 |
| Operating working capital | 322.7 | 432.6 |
| Current portion of long-term debt | (168.3) | (15.2) |
| Current portion of deferred reforestation | (32.5) | (34.4) |
| Income taxes recoverable | 47.1 | 136.7 |
| Net working capital | 531.4 | 815.2 |
| Long-term investments | 125.7 | 170.4 |
| Property, plant, equipment and timber | 1,798.5 | 1,959.4 |
| Goodwill | 85.7 | 69.2 |
| Deferred charges | 110.2 | 90.0 |
| Net assets | $ 2,651.5 | $ 3,104.2 |
| | | |
| Long-term debt | $ 428.7 | $ 481.6 |
| Deferred reforestation obligation | 63.1 | 65.6 |
| Other long-term provisions and accruals | 145.7 | 137.9 |
| Future income taxes – net | 242.4 | 299.5 |
| Non-controlling interests | 276.8 | 302.5 |
| Shareholders' equity | 1,494.8 | 1,817.1 |
| Total capitalization | $ 2,651.5 | $ 3,104.2 |
| | | |
| Ratio of current assets to current liabilities | 2.0 : 1 | 3.0 : 1 |
| Ratio of net debt to capitalization | 15% | 10% |

Canfor's ratio of current assets to current liabilities was 2.0:1 at the end of 2008, down from 3.0:1 at the end of 2007, mostly due to the reclassification of $168.3 million (2007 – $15.2 million) of long-term debt to current liabilities, and to a lesser extent, an increased drawdown of CPLP's operating loan, lower trade receivable and inventory levels (mostly reflecting weaker market conditions at the 2008 year end), and lower income taxes recoverable.

The Company's net debt to capitalization ratio was 15% at the end of 2008, up from 10% at the end of 2007, primarily due to the operating losses, asset impairments charges, foreign exchange translation losses on US dollar debt and losses on derivative financial instruments recorded in 2008. Shareholders' equity in 2008 included other comprehensive income of $53.5 million, substantially all of which related to foreign exchange gains on Canfor's self-sustaining foreign operations. In addition to the foreign exchange translation losses on US dollar debt, and the increased operating loan balance, net debt at the end of 2008 reflected positive cash flow from operating activities, which more than offset capital spending and cash distributions paid to non-controlling interests in 2008.

## CHANGES IN FINANCIAL POSITION

At the end of 2008, Canfor had $362.4 million of cash and cash equivalents.

| (millions of dollars, except for ratios) | 2008 | 2007 |
|---|---|---|
| Cash generated from (used in) | | |
| Operating activities | $ 157.7 | $ (483.1) |
| Financing activities | (42.4) | (174.3) |
| Investing activities | (48.4) | (70.9) |
| Increase (decrease) in cash and cash equivalents | $ 66.9 | $ (728.3) |

The changes in the components of these cash flows during 2008 are discussed below:

### OPERATING ACTIVITIES

In 2008, Canfor generated cash from operations of $157.7 million, compared to using $483.1 million in 2007. Cash generated in 2008 reflected reduced operating losses and a reduction in working capital balances, which included an income tax refund of $137.5 million related to previous period losses and lower trade receivables balances, partly offset by restructuring, mill closure and severance payments in 2008. The significant amount of cash used in operating activities in 2007 principally reflected the payment of income taxes and a special charge on duty refund monies and related interest, which were received by the Company in late 2006 following the implementation of the SLA. This was partly offset by a decrease in inventories in 2007.

### FINANCING ACTIVITIES

Financing activities in 2008 used net cash of $42.4 million in 2008 (2007 – $174.3 million). Payments included $52.3 million of CPLP distributions paid to non-controlling interests (2007 – $74.2 million) and the repayment of long-term debt of $14.8 million (2007 – $99.4 million). Partly offsetting these outflows was an increase of $25.2 million in CPLP's operating bank loan (2007 – decrease of $1.1 million).

### INVESTING ACTIVITIES

Cash used in investing activities amounted to $48.4 million in 2008 (2007 – $70.9 million). Property, plant and equipment additions were $80.2 million, of which approximately $30 million was spent to improve the Company's cost position, production and capacity. The balance was to maintain the existing productive capacity of the operations or to ensure Canfor's safety and environmental performance. Project spending in 2008 included work on fibre and energy optimization projects at the Company's Fort St. John mill, upgrades to the Conway mill in South Carolina, a replacement chip screening and in-feed system at CPLP's PG Pulp mill (mostly funded by insurance proceeds), and various upgrades at CPLP's Northwood and Intercon pulp mills. The Company received $30.0 million of initial advances from its insurer in relation to the NCP fire. Other outflows included an advance of $11.5 million to HSLP as part of a debt restructuring completed in early 2008.

In 2007, the Company's major investing activities were capital expenditures of $90.6 million and $16.8 million paid to acquire the Darlington sawmill. Temporary investments in 2007 increased by a net $38.6 million.

## FINANCIAL REQUIREMENTS AND LIQUIDITY

### OPERATING LOANS

At the end of 2008, the Company had $430.0 million of unsecured operating lines available (2007 – $409.0 million), of which $25.2 million was drawn down (2007 – nil) and $41.4 million was reserved for several standby letters of credit (2007 – $40.1 million).

Canfor Corporation's available operating line at December 31, 2008 was $355.0 million of which $17.3 million was reserved for several standby letters of credit, the majority of which related to unregistered pension plans. CPLP's available operating line was $75.0 million of which $25.2 million was drawn down and $24.1 million was reserved for a standby letter of credit issued to BC Hydro in connection with a 15 year electrical cogeneration agreement. These operating lines expire in June of 2011 and November of 2009, respectively.

On January 30, 2009, Canfor entered into two new operating loan facilities in the amounts of US$16.7 million ("Facility A") and US$43.7 million ("Facility B"). Facility A expires in January of 2012, with the option of four one-year extensions, and is non-recourse to Canfor, except for US$6.7 million. Facility B expires in January of 2011, with the option of five one-year extensions, and is non-recourse to Canfor under normal circumstances. The ABCP assets of the Company have been pledged as security to support these credit facilities.

### DEBT COVENANTS

Canfor has certain financial covenants on its debt obligations that stipulate maximum net debt to total capitalization ratios and minimum net worth amounts based on total shareholders' equity. The net debt to total capitalization is calculated by dividing total debt, less cash and cash equivalents, by shareholders' equity plus total debt less cash and cash equivalents. Debt obligations are held by various entities within the Canfor group and the individual debt agreements specify the entities within the group that are to be included in the covenant calculations. In certain circumstances, when net debt to total capitalization exceeds a certain threshold, Canfor is subject to an interest coverage ratio that requires a minimum amount of EBITDA relative to net interest expense.

In addition, CPLP has leverage and interest coverage ratios calculated by reference to operating earnings before interest, taxes, depreciation and amortization.

Provisions contained in Canfor's long-term borrowing agreements also limit the amount of indebtedness that the Company may incur and the amount of dividends it may pay on its common shares. The amount of dividends the Company is permitted to pay under its long-term borrowing agreements is determined by reference to consolidated net earnings less certain restricted payments.

Management reviews results and forecasts to monitor the Company's compliance with these covenant requirements. Canfor was in compliance with all its debt covenants for the year ended December 31, 2008.

### 2009 PROJECTED CAPITAL SPENDING AND DEBT REPAYMENTS

In 2009, depending on market conditions, Canfor anticipates that it may invest approximately $100 to $110 million in capital projects, which will consist of maintenance of business and improvement projects, several of which will be funded by the insurance proceeds from its NCP property damage claim. In March and April of 2009, $168.3 million (US$137.3 million) is required for scheduled long-term debt repayments. Canfor intends to finance its planned capital expenditures and scheduled debt repayments from existing cash reserves.

### COMMITMENTS

The following table summarizes Canfor's financial contractual obligations at December 31, 2008 for each of the next five years and thereafter:

| (millions of dollars) | 2009 | 2010 | 2011 | 2012 | 2013 | Thereafter | Total |
|---|---|---|---|---|---|---|---|
| Long-term debt and capital lease obligations | $ 168.3 | $ 40.1 | $ 100.8 | $ 61.2 | $ 226.6 | $ – | $ 597.0 |
| Operating leases | $ 22.4 | $ 13.8 | $ 6.6 | $ 4.7 | $ 2.7 | $ 1.8 | $ 52.0 |
| | $ 190.7 | $ 53.9 | $ 107.4 | $ 65.9 | $ 229.3 | $ 1.8 | $ 649.0 |

Other contractual obligations not included in the table above are:

- Purchase obligations and contractual obligations in the normal course of business. For example, purchase obligations of a more substantial dollar amount generally relate to the pulp business and are subject to "force majeure" clauses. In these instances, actual volumes purchased may vary significantly from contracted amounts depending on Canfor's requirements in any given year.
- Deferred reforestation, for which a liability of $95.6 million has been recorded at December 31, 2008 (2007 – $100.0 million). The reforestation liability is a fluctuating obligation, based on the volume of timber harvested. The future cash outflows are a function of the actual costs of silviculture programs and of harvesting at the time and are based on, among other things, the location of the harvesting.
- Obligations to pay pension and other post-employment benefits, for which a liability of $127.0 million has been recorded at December 31, 2008 (2007 – $114.0 million).

### SALE OF PANEL AND FIBRE MILL PROPERTY

On February 13, 2009, Canfor completed the sale of a property located at New Westminster, British Columbia, for gross proceeds of $47.5 million. The property was the site of Canfor's former Panel and Fibre operation, which was permanently closed at the beginning of 2008. The transaction will result in a pre-tax gain of approximately $44 million.

### PENSION OBLIGATIONS

The global financial and credit crisis has resulted in a sharp drop in the market value of equity investments around the world and also in the market value of Canfor's pension plan assets. For accounting purposes, the date at which the accrued benefit obligation and the fair value of the plan assets are measured (the "Measurement Date") is September 30th of each year. The declines in the value of the pension plan assets up until that date are included in the Company's funded deficit of $33.8 million as shown in the notes to the Company's 2008 consolidated financial statements. In accordance with Canadian GAAP the 2009 pension expense for accounting purposes will reflect plan assets and obligations and various assumptions, including estimated plan rates of return and discount rates, at the Measurement Date.

In the period between the Measurement Date and December 31, 2008, the value of the Company's pension plan assets declined a further 10% (approximately $43 million), and the discount rate increased over the same period. While these movements do not have any impact on the Company's 2008 year end balance sheet or the 2009 pension expense, the 2010 pension expense will be impacted as a result of the changes in market value of plan assets between measurement dates. A new funding valuation is currently scheduled to be performed as of December 31, 2009 when any changes to cash contributions required from 2010 onwards will be determined. The impact on required cash contributions to the plans could be material.

## TRANSACTIONS WITH RELATED PARTIES

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

### HOWE SOUND PULP AND PAPER LIMITED PARTNERSHIP ("HSLP")

HSLP is jointly owned by Canfor and Oji Paper Co., Ltd ("Oji") and operates the Port Mellon kraft pulp and newsprint mill. Canfor does not reflect its share of HSLP's results in its financial statements, as its investment in HSLP has been written off.

Canfor and Oji have a prepayment agreement with HSLP whereby the partners prepay HSLP in advance of the due date for receivables for pulp marketed, or to be marketed, and collected on their behalf. Canfor charges a market rate of interest to HSLP for the period paid in advance and the prepayment is covered by the assignment of current or future accounts receivable. The agreement provides for Oji to prepay up to a maximum amount of $60.0 million and Canfor to a maximum of $50.0 million, which is used as short-term operating funds by HSLP. In addition, Canfor has granted extended credit terms to HSLP up to a maximum of $10.0 million. Canfor, through CPLP, also markets the pulp production of HSLP for which it receives commissions under the terms of an agency sales agreement. Canfor also provides management, fibre supply and other services to HSLP at cost. At the end of 2008, Canfor had an unsecured receivables balance outstanding with HSLP of $31.4 million.

Coastal Fibre Limited Partnership ("CFLP"), jointly owned by Canfor and Oji, purchases chips for resale to HSLP under a long-term fibre agreement with Western Forest Products Limited ("WFP"), for which CFLP charges HSLP a commission. The related transactions and balances outstanding are proportionately consolidated in Canfor's financial statements. At year end, Canfor's share of the outstanding balance owing by HSLP was $9.5 million. In January of 2009, WFP defaulted on its three year rolling average minimum chip volume supply obligation, and subsequently entered into negotiations with CFLP to resolve this matter.

As a consequence of a debt restructuring agreement among HSLP, Canfor, Oji and a consortium of Japanese banks (the "Banks") in February of 2008, Canfor contributed additional funds to HSLP of $18.8 million, which were still outstanding at year end. These funds are secured by the assets of HSLP, subject to other security granted to the Banks and Oji. The repayment of these funds has priority over all other repayments, except a minimum bank debt repayment, from the annual free cash flow of HSLP.

### OTHER

Other related party transactions include:

1. The purchase of pulp chips and lumber, at market value, from Lakeland Mills Ltd. and Winton Global Lumber Ltd., in which Canfor holds a one-third equity interest; and
2. Shipping services provided to Canfor by Seaboard International Shipping Company, in which Canfor holds a minority interest.

Additional details are contained in note 26 to Canfor's 2008 consolidated financial statements.

## SELECTED QUARTERLY FINANCIAL INFORMATION

| | 2008 | | | | 2007 | | | |
|---|---|---|---|---|---|---|---|---|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| **Sales and income** (millions of dollars) | | | | | | | | |
| Sales | $ 588.7 | $ 668.0 | $ 706.4 | $ 648.5 | $ 711.0 | $ 837.4 | $ 876.6 | $ 850.6 |
| Operating (loss) income | $ (74.2) | $ 12.8 | $ 20.8 | $ (117.5) | $ (124.7) | $ (52.1) | $ (38.4) | $ (57.8) |
| Net (loss) income | $ (229.8) | $ (94.2) | $ 64.2 | $ (85.4) | $ (237.0) | $ (42.1) | $ (38.8) | $ (42.7) |
| Per common share (dollars) | | | | | | | | |
| Net (loss) income – basic and diluted | $ (1.61) | $ (0.66) | $ 0.45 | $ (0.60) | $ (1.66) | $ (0.30) | $ (0.27) | $ (0.30) |
| **Statistics** | | | | | | | | |
| Lumber shipments (MMfbm) | 956 | 906 | 1,107 | 1,023 | 1,149 | 1,301 | 1,345 | 1,213 |
| Plywood shipments (MMsf 3/8") | 28 | 54 | 96 | 86 | 90 | 90 | 119 | 87 |
| OSB shipments (MMsf 3/8") | 56 | 91 | 153 | 164 | 166 | 162 | 168 | 174 |
| Pulp shipments (000 mt) | 236 | 284 | 289 | 279 | 308 | 307 | 309 | 304 |
| Average exchange rate – US$/Cdn$ | $ 0.825 | $ 0.960 | $ 0.990 | $ 0.996 | $ 1.019 | $ 0.957 | $ 0.911 | $ 0.854 |
| Average Western SPF 2x4 #2&Btr lumber price (US$) | $ 190 | $ 263 | $ 230 | $ 205 | $ 230 | $ 260 | $ 258 | $ 253 |
| Average SYP (East) 2x4 #2 lumber price (US$) | $ 258 | $ 289 | $ 294 | $ 285 | $ 277 | $ 273 | $ 292 | $ 279 |
| Average plywood price – Toronto (Cdn$) | $ 336 | $ 333 | $ 337 | $ 347 | $ 374 | $ 394 | $ 357 | $ 379 |
| Average OSB price – North Central (US$) | $ 172 | $ 202 | $ 174 | $ 138 | $ 165 | $ 177 | $ 156 | $ 145 |
| Average NBSK pulp list price delivered to U.S. (US$) | $ 787 | $ 880 | $ 880 | $ 880 | $ 857 | $ 837 | $ 810 | $ 790 |

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

## THREE-YEAR COMPARATIVE REVIEW

| (millions of dollars, except per share amounts) | 2008 | 2007 | 2006 |
|---|---|---|---|
| Sales | $ 2,611.6 | $ 3,275.6 | $ 3,842.3 |
| Net (loss) income before discontinued items | $ (345.2) | $ (360.6) | $ 475.7 |
| Net (loss) income | $ (345.2) | $ (360.6) | $ 471.8 |
| Total assets | $ 3,200.4 | $ 3,507.8 | $ 4,663.5 |
| Total long-term financial liabilities | $ 428.7 | $ 481.6 | $ 602.8 |
| Net (loss) income before discontinued items per share, basic and diluted | $ (2.42) | $ (2.53) | $ 3.34 |
| Net (loss) income per share, basic and diluted | $ (2.42) | $ (2.53) | $ 3.31 |

## QUARTER ENDED DECEMBER 31, 2008 VS. QUARTER ENDED DECEMBER 31, 2007

### OVERVIEW OF OPERATING RESULTS

The Company recorded an operating loss of $74.2 million and a net loss of $229.8 million for the fourth quarter of 2008, compared with an operating loss of $124.7 million and a net loss of $237.0 million in the fourth quarter of 2007. The loss per share (basic and diluted) was $1.61 in the fourth quarter of 2008, compared to a loss per share of $1.66 in the fourth quarter of 2007.

The fourth quarter 2008 results include an asset impairment charge of $99.6 million ($74.1 million after taxes). An asset impairment charge of $256.0 million ($189.1 million after taxes) was recorded in the fourth quarter of 2007.

An overview of the results by business segment for the fourth quarter of 2008 compared to the fourth quarter of 2007 follows.

### LUMBER

SELECTED FINANCIAL INFORMATION AND STATISTICS – LUMBER

Summarized results for the Lumber segment for the fourth quarter of 2008 and 2007 were as follows:

| (millions of dollars, unless otherwise noted) | Q4 2008 | Q4 2007 |
|---|---|---|
| Sales | $ 363.9 | $ 395.3 |
| EBITDA[25] | $ (24.1) | $ (73.9) |
| Adjusted EBITDA | $ (20.4) | $ (66.9) |
| EBITDA margin[25] | (7)% | (19)% |
| Adjusted EBITDA margin | (6)% | (17)% |
| Operating loss[25] | $ (50.8) | $ (99.5) |
| Average SPF 2x4 #2 & Btr lumber price in US$[26] | $ 190 | $ 230 |
| Average SPF price in Cdn$ | $ 230 | $ 226 |
| Average SYP 2x4 #2 lumber price in US$[27] | $ 258 | $ 277 |
| Average SYP price in Cdn$ | $ 313 | $ 272 |
| Production – SPF lumber (MMfbm) | 791.6 | 866.8 |
| Production – SYP lumber (MMfbm) | 78.6 | 93.3 |
| Shipments – Canfor-produced SPF lumber (MMfbm)[28] | 834.3 | 988.4 |
| Shipments – Canfor-produced SYP lumber (MMfbm)[28] | 86.2 | 103.3 |
| Shipments – wholesale lumber (MMfbm) | 35.7 | 57.2 |

(25) EBITDA and Operating loss for the fourth quarter of 2008 include a log inventory write-down expense of $1.5 million, which resulted primarily from lower prices.
(26) Western Spruce/Pine/Fir, per thousand board feet (Source – Random Lengths Publications, Inc.)
(27) Southern Yellow Pine, Eastside, per thousand board feet (Source – Random Lengths Publications, Inc.)
(28) Includes shipments of lumber purchased for remanufacture.

## OVERVIEW

The Lumber segment reported an operating loss of $50.8 million for the fourth quarter of 2008, an improvement of $48.7 million compared to an operating loss of $99.5 million for the fourth quarter of 2007. Adjusted EBITDA improved by $46.5 million over the same period.

The improvement in Adjusted EBITDA reflected significantly lower unit manufacturing costs, achieved in the face of increased downtime in the current period. The fall in US dollar lumber prices between both quarters was offset by the decrease in the value of the Canadian dollar compared to the US dollar in the fourth quarter of 2008. Adjusted EBITDA was also positively impacted by the $10.8 million SLA Third Country Adjustment export tax refund receivable recorded in the fourth quarter of 2008.

## MARKETS

Demand for lumber in the U.S. continued to decline during the fourth quarter of 2008, with total U.S. housing starts dropping to 550,000 units SAAR[29] in December, the lowest level since the U.S. Bureau of the Census began recording in 1959. U.S. housing starts were down 495,000 units SAAR, or 43%, compared to the fourth quarter of 2007. Single family starts continued to fall sharply during the quarter, and were down 44% compared to the same quarter of 2007.

Inventories of new homes for sale at the end of the fourth quarter of 2008 were 12.9 months, up 3.1[29] months, compared to the fourth quarter of 2007 of 9.8 months; however inventories of existing homes were at 9.3[30] months, down slightly from 9.7 months at the end of 2007.

Canadian housing starts steadily declined throughout the quarter, averaging 190,000 units[31] SAAR, down 24,000 units, or 11%, compared to the fourth quarter of 2007.

Offshore demand remained relatively stable throughout the quarter. In Japan, a modest increase in 2x4 housing starts helped to offset an overall decline in construction activity.

## SALES

Lumber sales revenue for the fourth quarter of 2008 was down $31.4 million, or 8%, compared to the fourth quarter of 2007. Shipments were down 193 million board feet, or 17%, reflecting significant additional market-related curtailment in the fourth quarter of 2008.

The average price for all grades and widths of SPF and SYP lumber fell sharply compared to the fourth quarter of 2007. Lumber SPF prices, as measured by Western SPF 2x4 #2&Btr, were down US$40 per Mfbm, or 17%, compared to the fourth quarter of 2007 and average prices for SYP lumber, as measured by 2x4 #2&Btr, were down US$19 per Mfbm, or 7%, over the same period. Similar declines were recorded for wider widths. Canadian dollar sales realizations were positively impacted by a 19% increase in the average value of the US dollar compared to the same quarter a year ago.

The Random Lengths Framing Lumber Composite price averaged US$223 per Mfbm for the fourth quarter of 2008 (down US$41 per Mfbm compared to the comparative quarter in 2007), remaining well below the trigger price of US$315 per Mfbm required to reduce the export tax rate on all U.S. bound shipments below the current rate of 15%. In the fourth quarter of 2008, the Company recorded a recovery of $10.8 million in connection with the SLA Third Country Adjustment refund claim.

Total residual fibre sales revenue was in line with the fourth quarter of 2007, with a decrease in sales volumes being offset by an increase in chip prices.

## OPERATIONS

Lumber production for the fourth quarter was 870 million board feet, 90 million board feet, or 9%, lower than for the same quarter in 2007. Production for the current period reflected the indefinite closures of the Mackenzie and Chetwynd sawmills, as well as a reduced number of shifts. Production in the fourth quarter of 2008 also included the Darlington sawmill in South Carolina, which was acquired in late 2007.

Conversion costs were 7% lower than the same quarter of 2007, mainly due to increased productivity and cost reduction initiatives carried out in 2008. Log costs were also down significantly compared to the final quarter of 2007, primarily due to lower operating and overhead costs. Overall, the Company's unit cash manufacturing costs were down 12% relative to the fourth quarter of 2007.

(29) U.S. Census Bureau
(30) National Association of Realtors
(31) CMHC

## PANELS

### SELECTED FINANCIAL INFORMATION AND STATISTICS – PANELS

Summarized results for the Panels segment for the fourth quarter of 2008 and 2007 were as follows:

| (millions of dollars, unless otherwise noted) | Q4 2008 | Q4 2007 |
|---|---|---|
| Sales | $ 20.5 | $ 70.5 |
| EBITDA[32] | $ (10.9) | $ (28.8) |
| Adjusted EBITDA | $ (4.2) | $ (14.4) |
| EBITDA margin[32] | (53)% | (41)% |
| Adjusted EBITDA margin | (20)% | (20)% |
| Operating loss[32] | $ (15.2) | $ (34.2) |
| Average plywood price in Cdn$[33] | $ 336 | $ 374 |
| Average OSB price in US$[34] | $ 172 | $ 165 |
| Average OSB price in Cdn$ | $ 209 | $ 162 |
| Production – plywood (MMsf 3/8") | 13.8 | 93.1 |
| Production – OSB (MMsf 3/8") | 56.8 | 167.6 |
| Shipments – plywood (MMsf 3/8") | 28.2 | 90.3 |
| Shipments – OSB (MMsf 3/8") | 55.7 | 166.3 |

(32) EBITDA and Operating loss for the fourth quarter of 2008 include a log inventory write-down expense of $2.1 million, which resulted from higher log inventory volumes at the PV OSB mill at the end of the year.
(33) Canadian softwood plywood, per Msf 3/8" basis, delivered to Toronto (Source – C.C. Crowe Publications, Inc.)
(34) OSB, per Msf 7/16" North Central (Source – Random Lengths Publications, Inc.)

#### OVERVIEW

The Panels segment recorded an operating loss of $15.2 million for the fourth quarter, an improvement of $19.0 million compared to the fourth quarter of 2007. Adjusted EBITDA was up $10.2 million, primarily due to lower losses resulting from the indefinite idling of the PolarBoard and Tackama operations, as well as the increase in the average OSB price, which was up 29% in Canadian dollar terms compared to the fourth quarter of 2007.

Restructuring, mill closure and severance costs of $6.7 million were recorded in the Panels segment in the fourth quarter, principally as a result of the indefinite closure of Tackama. The fourth quarter of 2007's results reflected restructuring costs of $14.4 million related to the permanent closure of the Company's Panel and Fibre operation announced in late 2007.

#### MARKETS

Panel markets were weak in the fourth quarter of 2008, with sluggish activity reflecting the falloff in demand. OSB prices declined through the fourth quarter and ended the year at US$153 per Msf[35].

#### SALES

OSB prices averaged US$172 per Msf for the fourth quarter of 2008, up 4% from the fourth quarter of 2007, with Canadian softwood plywood 3/8" delivered Toronto price down $38, or 10%, over the same period. Total shipment volumes were down 67% compared to the fourth quarter of 2007, principally as a result of the NCP fire, the permanent closure of the Panel and Fibre operations in January, the indefinite closures of PolarBoard in June and Tackama in October, and curtailments at the PV OSB mill in the fourth quarter of 2008.

#### OPERATIONS

Production in the fourth quarter reflected significantly lower operating rates due to curtailment and closures, with volumes down 73% versus the fourth quarter of 2007. Unit cash manufacturing costs were up compared to the fourth quarter of 2007, reflecting the much lower operating rates. Increased wax and resin costs in 2008 also had a significant impact on costs when compared to the fourth quarter of 2007.

(35) Random Lengths

## PULP AND PAPER

### SELECTED FINANCIAL INFORMATION AND STATISTICS – PULP AND PAPER[36]

Summarized results for the Pulp and Paper segment for the fourth quarter of 2008 and 2007 were as follows:

| (millions of dollars, unless otherwise noted) | Q4 2008 | Q4 2007 |
|---|---|---|
| Sales | $ 204.3 | $ 245.2 |
| EBITDA | $ 8.9 | $ 27.7 |
| EBITDA margin | 4% | 11% |
| Operating (loss) income | $ (2.2) | $ 12.9 |
| Average pulp price delivered to U.S. – US$[37] | $ 787 | $ 857 |
| Average price in Cdn$ | $ 954 | $ 841 |
| Production – pulp (000 mt) | 256.1 | 313.2 |
| Production – paper (000 mt) | 30.1 | 33.1 |
| Shipments – Canfor-produced pulp (000 mt) | 235.6 | 308.3 |
| Pulp marketed on behalf of HSLP (000 mt)[38] | 52.6 | 93.3 |
| Shipments – paper (000 mt) | 24.3 | 32.4 |

(36) Includes the Taylor Pulp mill and 100% of CPLP, which is consolidated in Canfor's operating results. Pulp production and shipment volumes presented are for both NBSK pulp and BCTMP.
(37) Per tonne, NBSK pulp price delivered to U.S. (RISI)
(38) Howe Sound Pulp and Paper Limited Partnership Pulp mill

#### OVERVIEW

Compared to the same quarter of 2007, operating income and EBITDA were down $15.1 million and $18.8 million respectively. The significantly weaker Canadian dollar resulted in higher Canadian dollar sales realizations, but this benefit was more than offset by lower sales volumes, weaker global prices, increased scheduled maintenance outage costs, and higher freight and fibre costs in the fourth quarter of 2008.

#### MARKETS

World pulp markets continued to weaken through the fourth quarter. PPPC[39] reported total Global 100 chemical market pulp shipments in December of 2008 were at a rate of 88% of capacity compared to 94% for December of 2007. For NBSK market pulp, the shipment rate in December of 2008 was 83% of capacity compared to 95% for the same month in 2007.

As a result of the lower shipments, producer market pulp inventories increased during the fourth quarter of 2008, from 44 days to 46 days of supply for total chemical market pulp and from 36 days to 40 days of supply for softwood market pulp. By comparison, producer inventories at the end of 2007 were 29 days for total chemical pulp and 27 days of supply for softwood market pulp.

The decline in market pulp shipments was mainly caused by decreased demand for printing and writing papers, the largest consuming segment of market pulp. In particular, demand for printing and writing papers in North America declined by 19% compared to the fourth quarter of 2007.

As a result of the rapid decline in pulp demand, list prices in North American and European markets declined from US$875 per tonne and US$870 per tonne, respectively, at the end of 2007, to US$730 per tonne and US$635 per tonne at the end of 2008.

#### SALES

Shipments of Canfor-produced pulp were 236 million tonnes, down 73 million tonnes, or 24%, compared to shipments in the final quarter of 2007, for the most part reflecting the significantly lower sales activity in the fourth quarter of 2008. Realized Canadian dollar pulp prices showed a modest increase compared to the fourth quarter of 2007, primarily due to the impact of the weaker Canadian dollar, which more than offset lower global prices in US dollars.

(39) Pulp and Paper Products Council ("PPPC")

OPERATIONS

NBSK production during the fourth quarter was 42,000 tonnes lower than the fourth quarter of 2007. The reduced production primarily resulted from scheduled maintenance outages and market curtailment in the current quarter.

Compared to the same quarter of 2007, unit manufacturing costs were up significantly, principally due to lower production volumes, scheduled maintenance outage costs and higher fibre costs. The higher fibre costs resulted from increased prices for sawmill residual chips and a higher percentage of whole log chipping. Freight costs were also up over the fourth quarter of 2007.

## NON-SEGMENTED ITEMS

| (millions of dollars) | Q4 2008 | Q4 2007 |
|---|---|---|
| Corporate costs | $ (6.0) | $ (3.9) |
| Interest expense, net | $ (7.7) | $ (4.3) |
| Foreign exchange loss on long-term debt and investments, net | $ (72.0) | $ (4.1) |
| (Loss) gain on derivative financial instruments | $ (81.7) | $ 6.2 |
| Asset impairments | $ (99.6) | $ (256.0) |
| Other income (expense), net | $ 12.9 | $ (3.5) |

Corporate costs were $6.0 million in the fourth quarter of 2008, compared to $3.9 million in the fourth quarter of 2007, primarily due to the reversal of $2.3 million of long-term incentive compensation expense at the end of 2007.

Net interest expense of $7.7 million was recorded in the fourth quarter of 2008, compared with net interest expense of $4.3 million in the fourth quarter of 2007, reflecting higher net indebtedness in 2008.

A foreign exchange translation loss on the Company's US dollar denominated debt, net of investments, of $72.0 million was recorded in the fourth quarter of 2008 as a result of a 16.5 cent, or 16%, fall in the value of the Canadian dollar against the US dollar over the quarter.

The Company also recorded an $81.7 million loss related to the Company's derivative financial instruments in the fourth quarter of 2008. For the most part, this was due to the significant weakening of the Canadian dollar, but unrealized losses were also recorded on natural gas and diesel derivatives.

An asset impairment charge of $99.6 million was recorded in the fourth quarter of 2008. Of this amount, $83.4 million related substantially to impairment charges on the indefinitely idled Tackama and PolarBoard operations. The balance related to long-term investments, including a $10.2 million charge for the Company's non-bank asset-backed commercial paper. In the fourth quarter of 2007, the Company recorded an asset impairment charge of $256.0 million mostly related to capital assets in the Panels and Lumber segments.

## EBITDA RECONCILIATION AND SPECIFIC ITEMS AFFECTING COMPARABILITY

### EBITDA RECONCILIATION

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

| (millions of dollars) | 2008 | | | | 2007 | | | |
|---|---|---|---|---|---|---|---|---|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| **Net (loss) income, as reported** | $ (229.8) | $ (94.2) | $ 64.2 | $ (85.4) | $ (237.0) | $ (42.1) | $ (38.8) | $ (42.7) |
| Add (subtract): | | | | | | | | |
| Non-controlling interests | $ (12.6) | $ 5.4 | $ 9.2 | $ 22.0 | $ 6.1 | $ 16.9 | $ 18.1 | $ 24.3 |
| Income tax (recovery) expense | $ (80.2) | $ (30.0) | $ 24.0 | $ (55.7) | $ (155.3) | $ (27.2) | $ (25.6) | $ (26.0) |
| Other (income) expense | $ (12.9) | $ (0.1) | $ 1.5 | $ (1.2) | $ 3.3 | $ 9.3 | $ 13.7 | $ (15.3) |
| Asset impairments | $ 99.6 | $ 70.0 | $ – | $ – | $ 256.0 | $ 7.0 | $ – | $ 5.0 |
| Prince George Pulp & Paper mill fire, net | $ 0.3 | $ – | $ – | $ (8.5) | $ – | $ – | $ – | $ – |
| North Central Plywoods mill fire, net | $ – | $ – | $ (57.9) | $ – | $ – | $ – | $ – | $ – |
| Loss (gain) on derivative financial instruments | $ 81.7 | $ 38.8 | $ (26.0) | $ (6.0) | $ (6.2) | $ (8.9) | $ 7.7 | $ (8.5) |
| Foreign exchange loss (gain) on long-term debt and temporary investments, net | $ 72.0 | $ 16.2 | $ 0.1 | $ 12.0 | $ 4.1 | $ (9.5) | $ (16.8) | $ 6.0 |
| Interest expense, net | $ 7.7 | $ 6.7 | $ 5.7 | $ 5.3 | $ 4.3 | $ 2.4 | $ 3.3 | $ (0.6) |
| Amortization | $ 44.0 | $ 42.2 | $ 41.5 | $ 43.5 | $ 47.2 | $ 45.6 | $ 43.5 | $ 47.8 |
| EBITDA, as reported | $ (30.2) | $ 55.0 | $ 62.3 | $ (74.0) | $ (77.5) | $ (6.5) | $ 5.1 | $ (10.0) |
| Restructuring, mill closure and severance costs | $ 10.3 | $ 5.4 | $ 34.0 | $ 3.8 | $ 21.5 | $ 11.1 | $ 8.7 | $ – |
| **Adjusted EBITDA** | $ (19.9) | $ 60.4 | $ 96.3 | $ (70.2) | $ (56.0) | $ 4.6 | $ 13.8 | $ (10.0) |
| Log inventory (expense) recovery resulting from new inventory accounting standard included in EBITDA | $ (3.9) | $ 3.9 | $ 72.4 | $ (42.0) | $ – | $ – | $ – | $ – |

## SPECIFIC ITEMS AFFECTING COMPARABILITY OF NET LOSS

Factors that impact the comparability of the quarters are noted below:

| After-tax impact, net of non-controlling interests (millions of dollars, except for per share amounts) | 2008 | | | | 2007 | | | |
|---|---|---|---|---|---|---|---|---|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| **Net (loss) income, as reported** | $ (229.8) | $ (94.2) | $ 64.2 | $ (85.4) | $ (237.0) | $ (42.1) | $ (38.8) | $ (42.7) |
| Foreign exchange loss (gain) on long-term debt and temporary investments, net | $ 52.2 | $ 11.3 | $ – | $ 8.7 | $ 3.5 | $ (5.1) | $ (10.2) | $ 5.3 |
| Loss (gain) on derivative financial instruments | $ 50.3 | $ 21.4 | $ (14.5) | $ (2.7) | $ (3.5) | $ (6.9) | $ 3.7 | $ (4.9) |
| North Central Plywoods mill fire, net | $ – | $ – | $ (45.0) | $ – | $ – | $ – | $ – | $ – |
| Prince George Pulp & Paper mill fire, net | $ 0.2 | $ – | $ – | $ (3.6) | $ – | $ – | $ – | $ – |
| Asset impairments | $ 74.1 | $ 56.9 | $ – | $ – | $ 189.1 | $ 6.0 | $ – | $ 4.1 |
| New inventory accounting standard | $ 2.6 | $ (2.5) | $ (47.8) | $ 29.0 | $ – | $ – | $ – | $ – |
| Restructuring, mill closure and severance costs | $ 6.8 | $ 3.6 | $ 22.3 | $ 2.6 | $ 14.2 | $ 7.3 | $ 5.8 | $ – |
| Corporate income tax rate reductions | $ – | $ – | $ – | $ (9.1) | $ (35.8) | $ (0.9) | $ (1.0) | $ – |
| Other items | $ 0.1 | $ – | $ – | $ – | $ (0.1) | $ (4.2) | $ (2.3) | $ (2.5) |
| Net impact of above items | $ 186.3 | $ 90.7 | $ (85.0) | $ 24.9 | $ 167.4 | $ (3.8) | $ (4.0) | $ 2.0 |
| **Net loss, as adjusted** | $ (43.5) | $ (3.5) | $ (20.8) | $ (60.5) | $ (69.6) | $ (45.9) | $ (42.8) | $ (40.7) |
| **Net (loss) income per share (EPS), as reported** | $ (1.61) | $ (0.66) | $ 0.45 | $ (0.60) | $ (1.66) | $ (0.30) | $ (0.27) | $ (0.30) |
| Net impact of above items per share | $ 1.31 | $ 0.64 | $ (0.60) | $ 0.18 | $ 1.17 | $ (0.03) | $ (0.03) | $ 0.01 |
| **Net loss per share, as adjusted** | $ (0.30) | $ (0.02) | $ (0.15) | $ (0.42) | $ (0.49) | $ (0.33) | $ (0.30) | $ (0.29) |

## OUTLOOK

### LUMBER AND PANEL MARKETS

A turnaround in housing starts will remain the key indicator for improved demand for wood products. Although Canfor's business was initially impacted by the fall in U.S. housing starts, the global economic slowdown has started to affect lumber demand in all of Canfor's other major markets. A slow recovery of the U.S. housing industry is not projected before 2010, as homebuilders struggle to reduce their inventory of new homes. Housing prices must stabilize in order for consumer confidence to be restored. Canadian housing starts began to be affected by the global economic downturn towards the end of 2008, and starts below 185,000 are projected for 2009, compared to 211,000 for 2008.

The Repair and Remodeling and Do-It-Yourself sector is projected to be more negatively impacted in 2009 than it was in 2008 as home prices continue to fall and credit remains inaccessible to many homeowners or prospective buyers.

In Japan, housing starts are projected to decline in 2009. Demand from other offshore markets is also anticipated to slow down in the coming year. The Company anticipates its percentage of sales to China to continue to increase in 2009.

Similar to lumber, the panels market is projected to remain under pressure for 2009 due to the low housing start forecast and ongoing global economic declines.

In January, the Company took a further 29 million board feet of market curtailment and subsequently announced a further curtailment of 83 million board feet to occur in February, in addition to elimination of shifts at two of its sawmills for an indefinite period. Curtailment was also announced in February at the joint venture Peace Valley OSB mill.

### PULP AND PAPER MARKETS

Weak pulp markets are projected to continue through the first quarter of 2009 and to remain challenging for at least the first half of 2009.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements. Management regularly reviews these estimates and assumptions based on 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 Canfor's financial position.

### EMPLOYEE FUTURE BENEFITS

Canfor has various defined benefit and defined contribution plans providing both pension and other retirement benefits to most of its salaried employees and certain hourly employees not covered by forest industry union plans. Canfor also provides certain health care benefits and pension bridging benefits to eligible retired employees. The costs and related obligations of the pension and other retirement benefit plans are accrued in accordance with the recommendations of the Canadian Institute of Chartered Accountants ("CICA").

Canfor uses independent actuarial firms to perform actuarial valuations of the fair value of pension and other retirement benefit plan obligations. The application of these recommendations requires judgments regarding certain assumptions that affect the accrued benefit provisions and related expenses, including the discount rate used to calculate the present value of the obligations, the expected rate of return on plan assets, the rate of compensation increase and the assumed health care cost trend rates. Management and the Board of Directors' Pension Committee evaluate these assumptions annually based on experience and the recommendations of its actuarial firms. Changes in these assumptions result in actuarial gains or losses, which are amortized over the average remaining service period of the active employee group covered by the plans, only to the extent that the unrecognized net actuarial gains and losses are in excess of 10% of the greater of the accrued benefit obligations and the market-related value of plan assets.

The actuarial assumptions used in measuring Canfor's defined benefit plan are as follows:

| | 2008 | | 2007 | |
|---|---|---|---|---|
| (weighted average assumptions) | **Pension Benefit Plans** | **Other Benefit Plans** | Pension Benefit Plans | Other Benefit Plans |
| Accrued benefit obligation as of December 31: | | | | |
| Discount rate | **6.60%** | **6.70%** | 5.60% | 5.50% |
| Rate of compensation increase | **3.00%** | **n/a** | 3.00% | n/a |
| Benefit costs for year ended December 31: | | | | |
| Discount rate | **5.60%** | **5.50%** | 5.25% | 5.25% |
| Expected long-term rate of return on plan assets | **7.50%** | **n/a** | 7.00% | n/a |
| Rate of compensation increase | **3.00%** | **n/a** | 3.00% | n/a |

Assumed health care cost trend rates were as follows:

| (weighted average assumptions) | **2008** | 2007 |
|---|---|---|
| Initial health care cost trend rate | **5.83%** | 5.62% |
| Ultimate health care trend rate | **4.40%** | 4.27% |
| Year ultimate rate reached | **2014** | 2011 |

Assumed health care cost trend rates have a significant effect on the amounts reported for the other post-retirement benefit plans. A one percentage point change in assumed health care cost trend rates would have had the following impact on the amounts recorded in 2008:

| | 1% Increase | 1% Decrease |
|---|---|---|
| Increase (decrease) in accrued benefit obligation | $ 16.7 | $ (13.6) |
| Increase (decrease) in total service and interest cost | $ 2.3 | $ (1.8) |

See "Financial Requirements and Liquidity – Pension Obligations" section for discussion regarding the impact of the global financial and credit crisis on Canfor's pension plans and how this may affect Canfor's results and cash flows going forward.

### DEFERRED REFORESTATION

Canfor accrues an estimate of its future liability to perform forestry activities, defined to mean those silviculture treatments or activities that are carried out to ensure the establishment of a free-growing stand of young trees, including logging road rehabilitation. An estimate is recorded in the financial statements based on the number of hectares of timber harvested in the period and the estimated costs of fulfilling Canfor's obligation. Payments in relation to deforestation are expected to occur over periods of up to 18 years (the significant majority occurring in the first seven years) and have been discounted accordingly at rates of 4% to 7%. The actual costs that will be incurred in the future may vary based on, among other things, the actual costs at the time of harvesting.

### FUTURE INCOME TAXES

In accordance with CICA recommendations, Canfor recognizes future income tax assets when it is more likely than not that the future income tax assets will be realized. This assumption is based on management's best estimate of future circumstances and events. If these estimates and assumptions are changed in the future, the value of the future income tax assets could be reduced or increased, resulting in an income tax expense or recovery. Canfor reevaluates its future income tax assets on a regular basis.

### ASSET RETIREMENT OBLIGATIONS

Canfor records the estimated fair value of a liability for asset retirement obligations, such as landfill closures, in the period when a reasonable estimate of fair value can be made. For CPLP's landfill closure costs, the fair value is determined using estimated closure costs discounted over the estimated useful life. Payments relating to landfill closure costs are expected to occur at periods ranging from 32 to 40 years and have been discounted at rates ranging from 5.8% to 6.3%. The actual closure costs and periods of payment may differ from the estimates used in determining the year end liability. The fair value of the liability is added to the carrying amount of the associated asset and amortized over its useful life. The liability is accreted over time through changes to earnings and reduced by actual costs of settlement.

### ENVIRONMENTAL REMEDIATION COSTS

Costs associated with environmental remediation obligations are accrued and expensed when such costs are probable and can be reasonably estimated. Such accruals are adjusted as further information develops or circumstances change. Costs of future expenditures for environmental remediation obligations are discounted to their present value when the amount and timing of expected cash payments are reliably determinable.

### IMPAIRMENT OF GOODWILL

Goodwill, which is the excess of the purchase price paid for an acquisition over the fair value of the net assets acquired, is not amortized but is assessed annually for impairment, or more frequently if events or circumstances indicate that it may be impaired.

In order to assess the goodwill for impairment, an analysis of the future expected discounted cash flows of the assets to which the goodwill relates is prepared as and when required. As part of this process, assumptions are made in relation to forecast prices and exchange rates. Price forecasts are determined with reference to Resource Information Systems, Inc. ("RISI") publications and management estimates, and forecast exchange rates are based on forecasts from various recognized authorities. Given the inherent uncertainty regarding longer term prices and foreign exchange rates, management considers various possible scenarios and assigns probabilities to the likelihood of occurrence of each of these. The net present value of the future expected cash flows is compared to the carrying value of the Company's investment in these assets, including goodwill, at year end.

Based upon the analysis performed in 2008 the net present value of the estimated future discounted cash flows exceeded the value of the investment, and therefore no impairments to goodwill were required. However, if the U.S. and global economic downturn were to be longer or more severe than anticipated in the forecast assumptions, there is a possibility that an impairment of goodwill may be required in future periods.

## ASSET IMPAIRMENTS

As previously indicated, Canfor recorded the following asset impairment charges in 2008:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Capital assets | $ 77.2 | $ 231.4 |
| Assets related to Howe Sound Pulp and Paper Limited Partnership and Coastal Fibre Limited Partnership | $ 70.0 | $ 14.0 |
| Non-bank asset-backed commercial paper | $ 10.2 | $ 16.2 |
| Other | $ 12.2 | $ 6.4 |
| Total asset impairments | $ 169.6 | $ 268.0 |

### CAPITAL ASSETS

Canfor reviews the carrying values of its long-lived assets on a regular basis as events or changes in circumstances may warrant. Where the carrying value of assets is not expected to be recoverable from net future cash flows, they are written down to fair value. In view of the ongoing operating losses and expected market conditions, including exchange rates going forward, a review of the carrying value of all of the Company's sawmills and panelboard operations and various other assets was undertaken.

The first step in this process was to determine for each operation whether projected undiscounted net future cash flows from operations exceeded the net carrying amount of the assets as of the assessment date. For those operations where an impairment was indicated, the second step was to calculate the fair values using discounted net future cash flows expected from their use and eventual disposition.

Estimates of future cash flows used to test the recoverability of Canfor's long-lived assets generally include key assumptions related to forecast prices and exchange rates. Other significant assumptions are the estimated useful life of the long-lived assets, and the impacts of both the SLA with the U.S. and the Mountain Pine Beetle epidemic. Price forecasts beyond 2009 were determined with reference to RISI, and forecast exchange rates were based on forecasts from various recognized authorities. Given the importance of the US$/Cdn$ exchange rate in Canfor's business, where most sales are denominated in US dollars and most costs incurred in Canadian dollars, probabilities were assigned to the likelihood of occurrence of several exchange rate scenarios and a weighted average of these was used in determining the impairments to be recorded.

In some cases the future of these mills is uncertain (for example, whether they will be re-opened, sold or permanently shut-down). To account for this, management developed cash flows for each different scenario identified and applied a weighted average to determine the impairment to be recorded.

As a result of its assessment, Canfor recognized capital asset write-downs of $77.2 million related to property, plant and equipment and timber, all of which relates to the Panels segment. However, if the U.S. and global economic downturn were to be longer or more severe than anticipated in the forecast assumptions, there is a possibility that further impairment of capital assets may be required in future periods.

### ASSETS RELATED TO HOWE SOUND PULP AND PAPER LIMITED PARTNERSHIP AND COASTAL FIBRE LIMITED PARTNERSHIP

For the year ended December 31, 2008, an asset impairment charge of $70.0 million was recorded on assets related to HSLP and CFLP, which reflected current fair value, based on estimated future cash flows. Canfor's investments include a 50% interest in CFLP, an entity which supplies fibre and related services to HSLP. The impairment reflected the deterioration of B.C. Coastal pulp, paper and fibre market conditions.

### NON-BANK ASSET-BACKED COMMERCIAL PAPER

The ABCP of $69.3 million (US$56.6 million) is measured at the estimated fair value of Canfor's combined investments in asset-backed commercial paper of four different Canadian trusts (the "Trusts") with total original principal amount of US$81.2 million and original maturities between August and September of 2007.

Since August of 2007, there has been no active market for ABCP. The Trusts failed to make payment at maturity and, along with 16 other ABCP conduits, are subject to restructuring under the Pan-Canadian Investors Committee for Third Party structured Asset-Backed Commercial Paper (the "Pan-Canadian Investors Committee").

On March 17, 2008 the Pan-Canadian Investors Committee filed with the Ontario Superior Court of Justice a comprehensive arrangement pursuant to the Companies' Creditors Arrangement Act to restructure the affected trusts. The final restructuring plan was approved on January 12, 2009 and completed on January 21, 2009.

In the fourth quarter, an additional impairment of $10.2 million (US$8.4 million) was recorded on the ABCP based on the estimated fair value at year end, which took into account information available to Canfor related to its specific holdings of ABCP, and assumed a high likelihood of success for the proposed ABCP restructuring plan. The book value at December 31, 2008 reflected the impact of a weaker Canadian dollar on the US dollar denominated ABCP. No changes to fair value resulted from the completion of the restructuring plan after year end.

### OTHER

For the year ended December 31, 2008, other asset impairments of $12.2 million were recorded related to certain other investments and write-downs of spare parts inventory at indefinitely idled operations.

## VALUATION OF LOG AND FINISHED PRODUCT INVENTORIES

Solid wood inventories are written down to the lower of cost and net realizable value, which is determined by taking into account forecast prices and rates for the period over which the inventories are expected to be sold. Forecast prices are determined using RISI forecasts and management's estimates as at the year end, and may differ from the actual prices at which the inventories are sold. At the end of December 2008, the inventory balances included total write-downs of $46.2 million.

## ALLOWANCE FOR DOUBTFUL ACCOUNTS

An allowance for doubtful accounts of $3.0 million was recorded at December 31, 2008 (2007 – $0.4 million), which reflects management's assessment of risks attached to specific receivable balances. While significant bad debts have not been experienced in prior years, the additional provision is considered appropriate due to the current recession in the U.S. which may affect the ability of certain customers to pay amounts owed to the Company.

## INSURANCE PROCEEDS

The Company estimated the insurance property damage receivable in connection with the NCP fire in May using preliminary engineering estimates and other information available. This receivable was estimated on the basis that the insurance proceeds will be applied towards capital improvements at Canfor's other operations. Based on estimated insurance proceeds, net of an aggregate policy deductible of $2.4 million, and costs related to the fire, the Company recorded a pre-tax gain of $57.9 million. It is possible that future events, including the final negotiation of the insurance proceeds to be paid, may give rise to changes in the gain recorded in relation to these insurance claims.

CPLP estimated insurance property amounts receivable in connection with the PG Pulp mill fire using management's best estimates at year end of the final costs to complete construction of a replacement chip screening and in-feed system. In addition, amounts accrued for business interruption insurance receivable reflected management's best estimates with regards to the financial impact of lost production and other incremental costs covered under the policy. CPLP recorded a receivable of $12.2 million in relation to property damage, of which $11.2 million had been received, and $19.1 million in relation to business interruption, of which $15.2 million had been received. It is possible that future events, including the final negotiation of the insurance proceeds to be paid, may give rise to changes in the amounts recorded in relation to this.

## CHANGES IN ACCOUNTING POLICIES

### CAPITAL DISCLOSURES

Effective January 1, 2008, the Company adopted the CICA's new Handbook Section 1535 "Capital Disclosures". This Section establishes the standards for disclosing information about an entity's capital and how it is managed. Under this Section the Company is required to disclose qualitative information about its objectives, policies and processes for managing capital, quantitative data about what it regards as capital, whether it has complied with any externally imposed capital requirements and, if not, the consequences of such non-compliance.

### INVENTORIES – LOGS AND CAPITAL SPARES

The CICA issued a new Handbook Section 3031 "Inventories" which applied to Canfor as of January 1, 2008, and has been applied on retrospectively, without prior period restatement. This Section provides significantly more guidance on the measurement of inventories, with an expanded definition of cost, and the requirement that inventories must be measured at the lower of cost and net realizable value. Canfor had previously valued log inventories at the greater of net realizable value and replacement cost, if lower than average cost. In addition, the Section sets out additional disclosure requirements, including accounting policies, carrying values, and the amount of any inventory write-downs or reversal of any write-downs. In conjunction with Section 3061, "Property, Plant and Equipment", it also provides guidance on the classification of major spare parts and stand-by equipment.

As a result of implementing these standards, inventories decreased by $60.6 million (log inventories by $46.5 million, processing materials and supplies by $14.1 million), property, plant and equipment increased by $14.1 million, future income tax liabilities decreased by $15.9 million and opening retained earnings were reduced by $30.6 million.

### FINANCIAL INSTRUMENTS

The CICA issued two new Handbook Sections relating to financial instruments that were effective as of January 1, 2008. These are Section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation".

Section 3862 requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable the users to evaluate: (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks.

Section 3863 establishes standards for the presentation of financial instruments and non-financial derivatives.

As a result of these new standards, Canfor has provided additional disclosures in the financial statements.

### GOODWILL AND DEFERRED START-UP COSTS

In February of 2008, the CICA issued a new accounting standard, Handbook Section 3064 "Goodwill and Intangible Assets". This Section replaces Handbook Section 3062 "Goodwill and Intangible Assets" and Section 3450 "Research and Development Costs" and establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. Upon adoption of this new Standard, EIC 27 – "Revenues and Expenditures During the Pre-operating Period" is withdrawn and so various pre-production and start-up costs are required to be expensed as incurred. This Standard will be applicable to the Company for annual and interim periods beginning on January 1, 2009. The Company does not expect that this Section will have a material impact on its consolidated financial statements.

### INTERNATIONAL FINANCIAL REPORTING STANDARDS

In February of 2008, the Accounting Standards Board announced that publicly accountable entities will be required to prepare financial statements in accordance with International Financial Reporting Standards ("IFRS") for interim and annual periods in fiscal years beginning on or after January 1, 2011. More information on the adoption of IFRS can be found under "Conversion to International Financial Reporting Standards".

## RISKS AND UNCERTAINTIES

Risks and uncertainties fall into the general business areas of markets, international commodity prices, competition, currency exchange rates, environmental issues, forest land base, government regulations and policy reform, and, for Canadian companies, a history of trade disputes and issues and Aboriginal land claims. The future impact of the various uncertainties and potential risks described in the following paragraphs (together with the risks and uncertainties identified under each of the Company's business segments listed above) cannot be quantified or predicted with certainty. However, Canfor does not foresee unmanageable adverse effects on its business operations from, and believes that it is well positioned to deal with, such matters as may arise. The risks and uncertainties are set out in alphabetical order.

### ABORIGINAL ISSUES

Canadian judicial decisions have recognized the continued existence in the country of Aboriginal rights, including title, to lands continuously used or occupied by Aboriginal groups. Although Aboriginal groups have claimed Aboriginal rights over substantial portions of B.C. no Aboriginal right nor title has yet been determined in areas overlapping with Canfor's forest tenures and other operations. While uncertainty regarding property rights in Canada (including forest tenure and other resource rights) continues to exist, particularly in those areas where treaties have not been concluded with Aboriginal groups, such as much of B.C., the Government of B.C. has provided greater certainty for the forest industry by reaching agreements on forest resources with many bands. As a means of protecting treaty and aboriginal rights, as well as undetermined aboriginal rights, Canadian courts continue to confirm a duty to consult with Aboriginal groups when the Crown has knowledge of existing rights or the potential existence of an Aboriginal right, such as title, and contemplates conduct that might adversely impact them. The courts have not extended this duty to third parties, such as forest companies.

As issues relating to Aboriginal and treaty rights and consultation continue to be heard, developed and resolved in Canadian courts, Canfor will continue to cooperate, communicate and exchange information and views with Aboriginal groups and government, and participate with the Crown in its consultation processes with Aboriginal groups in order to foster good relationships and minimize risks to its tenures and operational plans. Due to their complexity, it is not expected that the issues regarding Aboriginal and treaty rights or consultation will be finally resolved in the short term and, accordingly, the impact of these issues on the timber supply from Crown lands and Canfor's tenures and on Canfor's operations is unknown at this time.

Canfor believes in building mutually beneficial and lasting relationships with local First Nations whose treaty rights or potential Aboriginal rights overlap with Canfor's areas of operations. Some of these relationships with Aboriginal people have been formalized through agreements that generally seek to increase First Nations' participation in Canfor's planning and harvesting activities while strengthening Canfor's access to fibre. Some relationships include support through Canfor scholarship programs, as well as mentoring opportunities and employment at our manufacturing and forestry operations. Canfor also has numerous business relationships ranging from short and long-term contracts with Aboriginal businesses to agreements to manage and purchase the timber from Forest Licenses held by local First Nations to jointly held Forest Licenses with local First Nations.

### ENVIRONMENTAL ISSUES

Canfor's operations are subject to environmental regulation by federal, provincial, state and local authorities, including specific environmental regulations relating to air emissions and pollutants, wastewater (effluent) discharges, solid waste, landfill operations, forestry practices, site remediation and the protection of endangered species and critical habitat. Canfor has incurred, and will continue to incur, capital expenditures and operating costs to comply with environmental laws and regulations. No assurance can be given that changes in these laws and regulations or their application will not have a material adverse effect on Canfor's business, operations, financial condition and operational results. Similarly, no assurance can be given that capital expenditures necessary for future compliance with existing and new environmental laws and regulations could be financed from Canfor's available cash flow. In addition, Canfor may discover currently unknown environmental issues, contamination, or conditions relating to its past or present operations. This may require site or other remediation costs to maintain compliance or correct violations or result in governmental or private claims for damage to person, property or the environment, which could have a material adverse effect on Canfor's business, financial condition and operational results.

Canfor has in place internal policies and procedures under which all its forestry and manufacturing operations are audited for compliance with laws and accepted standards and with its management systems. Canfor's woodlands operations in Canada are third-party certified to internationally-recognized sustainable forest management standards. Canfor's operations and its ability to sell its products could be adversely affected if those operations did not, or were perceived by the public as failing to, comply with applicable laws and standards, including responsible environmental and sustainable forestry standards.

## FINANCIAL RISK MANAGEMENT AND EARNINGS SENSITIVITIES

Demand for forest products, both wood products and pulp and paper, is closely related to global business conditions and tends to be cyclical in nature. Product prices can be subject to volatile change. Canfor, like the majority of the Canadian forest products industry, competes in a global market and the majority of its products are sold in US dollars. Consequently, changes in foreign currency relative to the Canadian dollar can impact Canfor's revenues and earnings.

### FINANCIAL RISK MANAGEMENT

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

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

#### (A) CREDIT RISK:

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

Financial instruments that are subject to credit risk include cash and cash equivalents, accounts receivable and long-term investments and other. Cash and cash equivalents includes cash held through major Canadian and international financial institutions and temporary investments with an original maturity date of three months or less.

Canfor utilizes a combination of credit insurance and self-insurance to manage the risk associated with trade receivables. Approximately 50% of the outstanding trade receivables are covered by credit insurance. Canfor's trade receivable balance at December 31, 2008 is $105.9 million, net of an allowance for doubtful accounts of $3.0 million. At December 31, 2008, approximately 98% of the trade accounts balance was within Canfor's established credit terms.

#### (B) LIQUIDITY RISK:

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

At December 31, 2008, Canfor has operating loans of $25.2 million, accounts payable and accrued liabilities of $322.9 million and current debt obligations of $168.3 million (US$137.3 million), all of which fall due for payment within one year of the balance sheet date.

#### (C) 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 and commodity prices.

(i) Interest Rate risk:

Canfor is exposed to interest rate risk through its current financial assets and financial obligations bearing variable interest rates. Canfor's cash and cash equivalents include term deposits with original maturity dates of three months or less.

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

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

(ii) Currency risk:

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

A portion of the currency risk associated with US dollar denominated sales is naturally offset by US dollar denominated expenses and the US dollar denominated debt. The majority of the remaining exposure is covered by option contracts (foreign exchange collars) that effectively limit the minimum and maximum Canadian dollar recovery related to the sale of those US dollars (See "Derivative Financial Instruments" section below).

(iii) Energy Price risk:

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

The exposure is hedged up to 100% through the use of floating to fixed swap contracts or option contracts with maturity dates up to a maximum of three years. In the case of diesel oil, Canfor uses heating oil contracts to hedge its exposure (See "Derivative Financial Instruments" section below).

(iv) Commodity Price risk:

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

Canfor had no futures contracts at December 31, 2008.

## DERIVATIVE FINANCIAL INSTRUMENTS

Subject to risk management policies approved by its Board of Directors, Canfor, from time to time, uses derivative instruments, such as forward exchange contracts and option contracts to hedge future movements of exchange rates and futures and forward contracts to hedge commodity prices. As December 31, 2008, the Company has the following derivatives:

- Foreign exchange forward contracts and collars of US$492.8 million (2007 – US$476.7 million). There were unrealized losses of $53.2 million (2007 – gains of $15.0 million) on the foreign exchange derivatives at the end of the year.
- Floating to fixed swaps that hedge future natural gas purchases of 6.9 million gigajoules (2007 – 10.1 million gigajoules). There were unrealized losses of $6.5 million (2007 – $5.7 million) on the natural gas swaps at the end of the year.
- Floating to fixed swaps that hedge future diesel purchases of 6.5 million gallons (2007 – 13.3 million gallons), plus a call option of 3.0 million gallons (2007 – nil). There were unrealized losses of $9.6 million (2007 – unrealized gains of $7.9 million) on the diesel swaps at the end of the year.

## SENSITIVITIES

Estimates of the sensitivity of Canfor's pre-tax results to currency fluctuations and prices for its principal products, based on 2009 forecast production and 2008 year end foreign exchange rates, are set out in the following table:

| (millions of dollars) | Impact on annual pre-tax earnings |
|---|---|
| Lumber (SPF) – US$10 change per Mfbm[40] | $ 34 |
| Lumber (SYP) – US$10 change per Mfbm[40] | $ 5 |
| OSB – US$10 change per Msf 3/8"[40] | $ 3 |
| Pulp – US$10 change per tonne[40, 41] | $ 9 |
| Canadian dollar – US$0.01 change per Canadian dollar: | |
| Operations[41] | $ 10 |
| US dollar denominated debt[41] | $ 6 |

(40) Based on sales of Canfor-produced product.
(41) Includes Canfor's 50.2% interest in CPLP.

## MARKET CONDITIONS

Prices for lumber and panels in 2007 and 2008 have reached historically low levels, which has resulted in significant operating losses and asset impairments incurred by the Company in those years. Should there be a protracted U.S. and global economic slowdown, there exists a risk that the Company may not remain in compliance with its debt covenants and would have to renegotiate the terms of its covenants with lenders.

## GOVERNMENT REGULATION

Canfor is subject to a wide range of general and industry-specific environmental, health and safety and other laws and regulations imposed by federal, provincial and local authorities, including those governing the use, storage, handling, generation, treatment, emission, release, discharge and disposal of certain hazardous materials and wastes, the remediation of contaminated soil and ground water and the health and safety of employees. If Canfor is unable to extend or renew a material approval, licence or permit required by such laws, or if there is a delay in renewing any material approval, licence or permit, Canfor's business, financial condition, results of operations and cash flows could be materially adversely affected. Future events such as any changes in these laws and regulations or any change in their interpretation or enforcement, or the discovery of currently unknown conditions, may give rise to additional expenditures or liabilities.

## INCOME TRUST TAXATION

On October 31, 2006 the Canadian Federal Government announced plans to apply a tax on distributions from publicly traded income trusts, such as the Canfor Pulp Income Fund. For existing income trusts, the government provided a four-year transition period, until the 2011 taxation year, before the tax would be applicable.

## LABOUR AGREEMENTS AND COMPETITION FOR PROFESSIONAL SKILLED LABOUR

Any labour disruptions and any costs associated with labour disruptions at Canfor's mills could have a material adverse effect on its production levels and results of operations. Canfor's various collective agreements with the USWA (United Steelworkers of America), the PPWC (Pulp, Paper and Woodworkers of Canada) and the CEP (Communications, Energy and Paperworkers Union) have terms expiring in June of 2009 (USW-Interior B.C.), January of 2010 (USW-Uneeda) and February of 2010 (CEP) respectively. Any future inability to negotiate acceptable contracts could result in a strike or work stoppage by the affected workers and increased operating costs as a result of higher wages or benefits paid to unionized workers.

Market conditions may cause shortages of both professional and skilled labour, which could have an adverse impact on the operation and management of Canfor's facilities.

## MAINTENANCE OBLIGATIONS AND FACILITY DISRUPTIONS

Canfor's manufacturing processes are vulnerable to operational problems that could impair Canfor's ability to manufacture its products. Canfor could experience a breakdown in any of its machines, or other important equipment, and from time to time, planned or unplanned maintenance outages that cannot be performed safely or efficiently during operations must be conducted. Such disruptions could cause a significant loss of production, which could have a material adverse effect on Canfor's business, financial condition and operating results.

## MOUNTAIN PINE BEETLE

On May 7, 2008 the government of B.C. released a document entitled Provincial-Level Projection of the Current Mountain Pine Beetle Outbreak. The B.C. government reported that the Mountain Pine Beetle has attacked approximately 620 million cubic metres of lodgepole pine. This represents approximately 46% of total merchantable pine volume on the Timber Harvesting Land Base (1.35 billion $m^3$). The government also projected that up to 76% of the pine volume in the "pine units" will be killed by 2015 if the infestation continues to behave as it has over the past eight years.

Government 2008 aerial survey results indicate that progress has been made in managing Mountain Pine Beetle in the central and northern areas of Alberta, particularly within the leading edge zone of the infestation. While pockets of high beetle populations continue to exist in Alberta, infestations are generally on the decline in northern areas. This is not the case for the southern portions of the province, where populations are still increasing.

The Alberta government has indicated its intention to continue providing emergency funding for Mountain Pine Beetle management programs in 2009.

In response to the infestation, B.C.'s provincial government increased the allowable annual cut ("AAC") levels in the heavily affected timber supply areas. The increase is designed to salvage as much of the dead and damaged lodgepole pine timber as possible, and to redirect harvesting in an attempt to reduce the spread of the beetle. As a result, Canfor has also significantly increased its harvest of dead pine within its Vanderhoof, Quesnel and Prince George operating areas.

A recent timber supply study conducted by the Council of Forest Industries analyzed the general trends of the Mountain Pine Beetle outbreak and forecasted the expected impacts on AAC. The study predicts that the timber supply areas surrounding Vanderhoof and Quesnel will experience a significant reduction in AAC in the next 10 to 15 years. This reduction is expected because these timber supplies consist of over 60% mature lodgepole pine that is either dead or at risk of attack and the remaining stands of Spruce, Balsam fir and Douglas fir are insufficient to support historic harvest levels. The timber supplies surrounding Prince George and Mackenzie have the advantage of larger log diameter and a large inventory of non-pine species. As a result, there is more flexibility in these timber supply areas to harvest other stands while the pine sites recover from the infestation. The study also predicts that most of the damaged pine volume in these areas could be recovered, which may in turn mitigate the need for a significant reduction in harvest levels. As a result, the study predicts that in 10 to 15 years the AAC in the Prince George timber supply areas will likely reduce to slightly below historic levels, and in the Mackenzie areas the AAC will remain unchanged. Other timber supply areas where Canfor has operating areas, such as in Fort Nelson, Fort St. John, and Chetwynd, are not expected to experience a reduction in harvest levels resulting from the current Mountain Pine Beetle infestation.

The Chief Forester for the Province of B.C. determines how much wood can be harvested in each of the province's 37 timber supply areas and 33 tree farm licences at least once every five years. The Prince George Timber supply review is presently being undertaken by the Province's Chief Forester.

A major assumption about the impact on harvest levels is the shelf life of the dead lodgepole pine. Shelf life represents the length of time the timber is commercially viable for sawlogs. Once the shelf life has passed for sawlogs, the volume may still be useable for chips or other non sawlog products. One of the determining factors that contribute to shelf life is the moisture content of the log and the moisture condition of the area where the timber is located. The impact of moisture variability on the shelf life of timber is still being studied, but indications are that sawlog shelf-life can vary from 3 to over 15 years depending on moisture levels. For the alternative products the shelf life is expected to be much longer. The reality about shelf life however, is that it is also largely a function of economic factors.

In the short term, the impact of the infestation on Canfor is manageable. By applying new technology and best practices the Company will continue to operate in the dead stands. However, given the nature and extent of the infestation, the long-term operational and financial impact on Canfor may be significant.

### OBLIGATIONS TO BC HYDRO

In 2003, Canfor entered into an agreement with BC Hydro to build an electrical cogeneration facility at the PG Pulp mill. Under the agreement, BC Hydro contributed $45.8 million of the project costs, with Canfor contributing the balance. The agreement was assigned to CPLP effective July 1, 2006, with incentive payments totaling $11.4 million outstanding. The final incentive payment of $11.4 million was received August 9, 2006, and transferred to Canfor. The total incentive payments of $45.8 million were accounted for as a credit to property plant and equipment of CPLP. The agreement entails a 15 year commitment with BC Hydro for power displacement at the cogeneration facility, whereby a proportionate repayment is required should the facility not generate the minimum of 390 gigawatt hours of electricity per year. Under the agreement, CPLP is required to post a letter of credit as security in annually decreasing amounts as the minimum required amount of electricity is generated.

As of December 31, 2008, CPLP has no repayment obligation under the terms of the agreement and a standby letter of credit in the amount of $24.1 million was issued to BC Hydro.

### RESIDUAL FIBRE REVENUES

Wood chips are a by-product of Canfor's lumber manufacturing process and are primarily sold to CPLP. These chips are the principal raw material utilized by CPLP in its pulp manufacturing operations. Canfor has a Fibre Supply Agreement with CPLP, which contains a pricing formula that currently results in CPLP paying Canfor market prices for wood chips and also contains a provision to adjust the pricing formula to reflect market conditions. Canfor currently provides approximately 64% of CPLP's chip requirements. If lumber market conditions are such that Canfor is unable to provide the current volume of chips to CPLP as a result of sawmill closures, whether temporary or permanent, CPLP's financial results could be materially affected. Similarly, if CPLP were to cease pulp operations for an extended period of time, Canfor would have a limited market for its chip supply and this could affect its ability to run the sawmills economically.

### SOFTWOOD LUMBER AGREEMENT – SURGE MECHANISM

The SLA includes a "Surge Mechanism", which increases the export tax rate for the month by 50% when the monthly volume of exports from a region exceeds a certain "Trigger Volume" as defined in the SLA. In 2008, the Company paid surge tax of $0.3 million on shipments from Alberta, Canada.

In 2007, the U.S. Coalition for Fair Lumber Imports alleged that U.S. consumption figures used in calculating the allowable exports in a month should not be the estimated or expected consumption but rather the actual consumption based on a 12-month rolling average. On that basis, Canfor would have been liable under the surge mechanism to pay approximately $16 million of additional cumulative export tax. Canada maintained that the U.S. was wrongly interpreting the point at which the surge clause is triggered. In early 2008, the London Court of International Arbitration ruled in favour of Canada and determined that no additional cumulative export tax liability was payable.

### STUMPAGE RATES

The B.C. government introduced a Market Pricing System ("MPS") for the B.C. Interior on July 1, 2006. Canfor is actively participating in discussions on MPS with the Ministry of Forests, which is scheduled for its fourth annual update on July 1, 2009. Canfor will continue to seek to manage and reduce the stumpage costs for its Interior operations under the stumpage appraisal system. The near-term imperative is to ensure that the stumpage system accurately reflects the market value of timber and is responsive to the deteriorating quality of the beetle-impacted fibre.

### TRANSPORTATION SERVICES

Canfor relies primarily on third parties for transportation of its products, as well as delivery of raw materials, a significant portion of which are transported by railroad, trucks and ships. If any of Canfor's third party transportation providers were to fail to deliver the raw materials or products or distribute them in a timely manner, Canfor may be unable to sell those products at full value, or at all, or unable to manufacture its products in response to customer demand, which could have a material adverse effect on Canfor's financial condition and operating results. In addition, if any of these third parties were to cease operations or cease doing business with Canfor, Canfor may be unable to replace them at reasonable cost.

## OUTSTANDING SHARE DATA

At February 19, 2009, there were 142,589,312 common shares issued and outstanding. In addition, at February 19, 2009, there were 200,468 stock options outstanding with exercise prices ranging from $8.30 to $11.80 per share.

## DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company has established disclosure controls and procedures to ensure that information disclosed in this MD&A and the related financial statements was properly recorded, processed, summarized and reported to the Board and the Audit Committee. The Company's chief executive officer ("CEO") and chief financial officer ("CFO") have evaluated the effectiveness of these disclosure controls and procedures for the period ending December 31, 2008, and have concluded that they are effective.

The CEO and CFO acknowledge responsibility for the design of internal controls over financial reporting ("ICFR"), and confirm that there were no changes in these controls that occurred during the most recent interim period ended December 31, 2008 which materially affected, or are reasonably likely to materially affect, the Company's ICFR. Based upon their evaluation of these controls for the year ended December 31, 2008, the CEO and CFO have concluded that these controls are operating effectively.

## CONVERSION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

In February of 2008, the Accounting Standards Board announced that publicly accountable entities will be required to prepare financial statements in accordance with International Financial Reporting Standards ("IFRS") for interim and annual periods in fiscal years beginning on or after January 1, 2011.

The Company has developed a conversion implementation plan to ensure that differences between Canadian GAAP and IFRS that affect Canfor are identified, and any required changes to accounting processes and controls (including information technology systems) are made in a timely manner to ensure a smooth transition to IFRS on January 1, 2010.

The key elements of the conversion implementation plan are as follows:

### PROJECT STRUCTURE

The Company has appointed a dedicated project manager to lead the conversion to IFRS. The project manager is working with other members of the finance team to execute the elements of the implementation plan. An implementation team is working closely with senior management in a number of different business areas to ensure that the impacts of the conversion throughout the business are managed in a timely and efficient manner. A steering committee has been established to oversee the project.

### PROCESS AND TIMING

The process of converting to IFRS has been divided into a number of different stages, many of which will run concurrently. The planning phase has now been completed, as has an initial diagnostic. A detailed review of the impact of IFRS on Canfor's consolidated financial statements, and other areas of the Company, is underway.

It is currently anticipated that the detailed diagnostic will be completed by mid-2009. Any changes required to systems and controls (including information technology systems) will be identified as the project progresses; these are currently projected to be designed and tested by the end of the third quarter of 2009. The implementation of any significant changes to systems and controls, as well as related training, is currently scheduled for the second half of 2009.

A draft opening balance sheet prepared under IFRS at the date of transition (January 1, 2010) is currently planned to be completed in the first half of 2010. Draft financial statements and disclosure information will be prepared for each quarter in 2010 (to be used for comparative purposes in 2011) and reporting under IFRS will commence for interim and annual periods in 2011.

### PROGRESS TO DATE

At December 31, 2008, the Company has completed the planning phase of the project and the initial diagnostic between Canadian GAAP and IFRS. While the effects of IFRS have not yet been fully determined, the Company has identified a number of key areas where it is likely to be impacted by changes in accounting policy. These include:

- Employee future benefits
- Property, plant, equipment and timber
- Intangible assets
- Impairment of assets
- Provisions, including deferred reforestation obligations and asset retirement obligations
- Presentation of financial statements, including presentation of minority interests

A detailed diagnostic is underway, and no decisions have yet been made with regard to accounting policy choices.

As a first-time adopter of IFRS, the Company is required to apply IFRS 1 "First time adoption of International Financial Reporting Standards". A number of exemptions are available under this Standard which the Company is currently evaluating. The more significant exemptions include: recognizing through opening retained earnings all cumulative actuarial gains and losses on employee benefit plans, and cumulative translation adjustments on self sustaining operations; avoiding a retroactive restatement of previous business combinations under IFRS; and electing to use fair value at the transition date as deemed cost for capital assets in certain circumstances.

Additional information about the Company, including its 2008 Annual Information Form, is available at www.sedar.com or at www.canfor.com.

## MANAGEMENT'S RESPONSIBILITY

The information and representations in the following 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 accounting principles generally accepted in Canada 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. Management does not believe it is likely that any differences will be material.

Canfor maintains systems of internal accounting controls, 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 Committee meets periodically throughout the year with management, external auditors and internal auditors to review their respective responsibilities, results of the reviews of internal accounting controls, 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, which recommended their approval by the Board of Directors. The consolidated financial statements have been audited by PricewaterhouseCoopers LLP, the external auditors, whose report follows.

February 19, 2009

James F. Shepard
President and
Chief Executive Officer

Thomas Sitar
Vice-President Finance and
Chief Financial Officer

## AUDITORS' REPORT

**To the Shareholders of Canfor Corporation**

We have audited the consolidated balance sheets of Canfor Corporation as at December 31, 2008 and 2007 and the consolidated statements of loss, changes in shareholders' equity and comprehensive loss and cash flows for each of the years in the two year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and its cash flows for each of the years in the two year period ended December 31, 2008 in accordance with Canadian generally accepted accounting principles.

February 19, 2009

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants
Vancouver, BC

# CONSOLIDATED BALANCE SHEETS

| As at December 31 (millions of dollars) | 2008 | 2007 |
|---|---|---|
| **ASSETS** | | |
| **Current assets** | | |
| Cash and cash equivalents | $ 362.4 | $ 295.5 |
| Accounts receivable (Note 4) | | |
| Trade | 105.9 | 199.5 |
| Other | 93.7 | 74.3 |
| Income taxes recoverable | 47.1 | 136.7 |
| Future income taxes, net (Note 22) | 31.2 | – |
| Inventories (Note 5) | 404.9 | 472.0 |
| Prepaid expenses | 35.1 | 40.8 |
| Total current assets | 1,080.3 | 1,218.8 |
| **Long term investments and other** (Note 6) | 125.7 | 170.4 |
| **Property, plant, equipment and timber** (Note 7) | 1,798.5 | 1,959.4 |
| **Goodwill** (Note 1) | 85.7 | 69.2 |
| **Deferred charges** (Note 8) | 110.2 | 90.0 |
| | $ 3,200.4 | $ 3,507.8 |
| **LIABILITIES** | | |
| **Current liabilities** | | |
| Operating loans (Note 9) | $ 25.2 | $ – |
| Accounts payable and accrued liabilities (Note 10) | 322.9 | 335.0 |
| Current portion of long-term debt (Note 11) | 168.3 | 15.2 |
| Current portion of deferred reforestation obligation (Note 13) | 32.5 | 34.4 |
| Future income taxes, net (Note 22) | – | 19.0 |
| Total current liabilities | 548.9 | 403.6 |
| **Long-term debt** (Note 11) | 428.7 | 481.6 |
| **Long-term accrued liabilities and obligations** (Note 12) | 208.8 | 203.5 |
| **Future income taxes, net** (Note 22) | 242.4 | 299.5 |
| **Non-controlling interests** | 276.8 | 302.5 |
| | $ 1,705.6 | $ 1,690.7 |
| **SHAREHOLDERS' EQUITY** | | |
| Share capital (Note 16) | $ 1,124.7 | $ 1,124.7 |
| Contributed surplus | 31.9 | 31.9 |
| Retained earnings | 316.7 | 692.5 |
| Accumulated other comprehensive income (loss) | 21.5 | (32.0) |
| Total shareholders' equity | 1,494.8 | 1,817.1 |
| | $ 3,200.4 | $ 3,507.8 |

**Commitments and contingencies** (Note 30)

**Subsequent events** (Note 31)

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

APPROVED BY THE BOARD

Director, R.L. Cliff

Director, J.F. Shepard

| Years ended December 31 (millions of dollars) | 2008 | 2007 |
|---|---|---|
| **Sales** | $ 2,611.6 | $ 3,275.6 |
| **Costs and expenses** | | |
| Manufacturing and product costs | 1,953.1 | 2,583.6 |
| Freight and other distribution costs | 476.2 | 565.0 |
| Export taxes (Note 4) | 55.1 | 101.8 |
| Amortization | 171.2 | 184.1 |
| Selling and administration costs | 60.6 | 72.8 |
| Restructuring, mill closure and severance costs (Note 18) | 53.5 | 41.3 |
| | 2,769.7 | 3,548.6 |
| **Operating loss** | (158.1) | (273.0) |
| Interest expense, net (Note 19) | (25.4) | (9.4) |
| Foreign exchange (loss) gain on translation of long-term debt and investments, net | (100.3) | 16.2 |
| (Loss) gain on derivative financial instruments (Note 25) | (88.5) | 16.0 |
| North Central Plywoods mill fire, net (Note 4) | 57.9 | – |
| Prince George Pulp & Paper mill fire, net (Note 4) | 8.2 | – |
| Asset impairments (Note 20) | (169.6) | (268.0) |
| Other income (expense), net (Note 21) | 12.7 | (11.1) |
| Net loss before income taxes and non-controlling interests | (463.1) | (529.3) |
| Income tax recovery (Note 22) | 141.9 | 234.1 |
| Non-controlling interests | (24.0) | (65.4) |
| **Net loss** | $ (345.2) | $ (360.6) |
| **Per common share (in dollars)** (Note 23) | | |
| Net loss – Basic and Diluted | $ (2.42) | $ (2.53) |

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

## CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE LOSS

| As at December 31 (millions of dollars) | 2008 | 2007 |
|---|---|---|
| **Consolidated Statements of Changes in Shareholders' Equity** | | |
| **Share capital** | | |
| Balance at beginning of year (Note 16) | $ 1,124.7 | $ 1,124.3 |
| Common shares issued on exercise of stock options (Note 17) | – | 0.4 |
| Balance at end of year | $ 1,124.7 | $ 1,124.7 |
| **Contributed surplus** | | |
| Balance at beginning and end of year | $ 31.9 | $ 31.9 |
| **Retained earnings** | | |
| Balance at beginning of year | $ 692.5 | $ 1,068.5 |
| Implementation of financial instruments standards (Note 2) | – | (13.2) |
| Change in accounting for Canfor Pulp Limited Partnership's pension liability | – | (2.2) |
| Change in accounting for inventories (Note 2) | (30.6) | – |
| Net loss for the year | (345.2) | (360.6) |
| Balance at end of year | $ 316.7 | $ 692.5 |
| **Accumulated other comprehensive income (loss)** | | |
| Balance at beginning of year | $ (32.0) | $ – |
| Implementation of financial instruments standards (Note 2) | – | (1.9) |
| Reclassification of foreign exchange translation adjustment | – | 3.0 |
| Net change in foreign exchange translation adjustment on self-sustaining foreign subsidiaries | 54.2 | (35.7) |
| Reclassification to income of (losses) gains on derivative instruments designated as cash flow hedges in prior years | (0.7) | 2.6 |
| Balance at end of year | $ 21.5 | $ (32.0) |
| **Total shareholders' equity – Balance at end of year** | $ 1,494.8 | $ 1,817.1 |
| **Consolidated Statement of Comprehensive Loss** | | |
| Net loss for the year | $ (345.2) | $ (360.6) |
| **Other comprehensive income (loss)** | | |
| Net change in foreign exchange translation adjustment on self-sustaining foreign subsidiaries | 54.2 | (35.7) |
| Reclassification to income of (losses) gains on derivative instruments designated as cash flow hedges in prior years | (0.7) | 2.6 |
| Other comprehensive income (loss) | $ 53.5 | $ (33.1) |
| **Total comprehensive loss** | $ (291.7) | $ (393.7) |

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

| Years ended December 31 (millions of dollars) | 2008 | 2007 |
|---|---|---|
| **Cash generated from (used in)** | | |
| **Operating activities** | | |
| Net loss for the year | $ (345.2) | $ (360.6) |
| Items not affecting cash: | | |
| Amortization | 171.2 | 184.1 |
| Income taxes | (43.5) | (111.9) |
| Long-term portion of deferred reforestation | (2.5) | (5.3) |
| North Central Plywoods mill fire, net (Note 4) | (57.9) | – |
| Prince George Pulp & Paper mill fire, net (Note 4) | (8.2) | – |
| Foreign exchange loss (gain) on translation of long-term debt | 115.2 | (92.5) |
| Loss (gain) on derivative financial instruments (Note 25) | 88.5 | (16.0) |
| Asset impairments (Note 20) | 169.6 | 268.0 |
| Non-controlling interests | 24.0 | 65.4 |
| Other | 3.9 | 40.6 |
| | 115.1 | (28.2) |
| Net proceeds from replacement of derivative financial instruments | 11.0 | – |
| Salary pension plan contributions | (15.9) | (21.7) |
| Deferred scheduled maintenance spending | (8.7) | (4.7) |
| Net change in non-cash working capital (Note 24) | 56.2 | (428.5) |
| | 157.7 | (483.1) |
| **Financing activities** | | |
| Proceeds from long-term debt | – | 0.3 |
| Repayment of long-term debt | (14.8) | (99.4) |
| Increase (decrease) in operating loans (Note 9) | 25.2 | (1.1) |
| Cash distributions paid to non-controlling interests | (52.3) | (74.2) |
| Other | (0.5) | 0.1 |
| | (42.4) | (174.3) |
| **Investing activities** | | |
| Decrease in temporary investments | – | 124.5 |
| Reclassification of non-bank asset-backed commercial paper | – | (85.9) |
| Business acquisitions (Note 3) | (0.8) | (16.8) |
| Additions to property, plant, equipment and timber | (80.2) | (90.6) |
| Proceeds from disposal of property, plant and equipment | 5.6 | 4.0 |
| Partial proceeds from North Central Plywoods mill fire claim (Note 4) | 30.0 | – |
| Partial proceeds from Prince George Pulp & Paper mill fire damage claim (Note 4) | 9.5 | – |
| Advances to affiliated companies | (11.5) | – |
| Other | (1.0) | (6.1) |
| | (48.4) | (70.9) |
| **Increase (decrease) in cash and cash equivalents** | 66.9 | (728.3) |
| **Cash and cash equivalents at beginning of year** | 295.5 | 1,023.8 |
| **Cash and cash equivalents at end of year** | $ 362.4 | $ 295.5 |
| | | |
| **Cash (payments) receipts in the year** | | |
| Interest, net | $ (26.6) | $ (25.3) |
| Income taxes | $ 137.5 | $ (230.5) |

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

December 31, 2008 and 2007

## 1. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements of Canfor Corporation (the "Company") are expressed in Canadian dollars and are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP").

### BASIS OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its subsidiaries, hereinafter referred to as "Canfor". Significant subsidiaries include 100% of Canadian Forest Products Ltd., 100% of New South Companies Inc., and 50.2% of Canfor Pulp Limited Partnership ("CPLP"). Investments over which the Company exercises significant influence are accounted for using the equity method, in which the original investment is recorded at cost and is subsequently adjusted for Canfor's share of post acquisition earnings. Joint ventures, which include Canfor-LP OSB Limited Partnership ("Canfor-LP OSB") and Coastal Fibre Limited Partnership ("CFLP") are proportionately consolidated (Note 27). Investments over which Canfor does not exercise significant influence are accounted for using the cost method, in which the original investment is recorded at cost and investment income distributions are recorded in the Consolidated Statements of Loss.

### USE OF ESTIMATES

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Canfor regularly reviews its estimates and assumptions, however, it is possible that circumstances may arise which cause actual results to differ from management estimates, and these differences could be material.

Significant areas requiring the use of management estimates are deferred reforestation costs, inventory valuations, amortization rates, asset retirement obligations, environmental remediation costs, provisions for insurance claims, pension and other benefit plan assumptions, and the valuation of goodwill, long-lived assets, investments, and non-bank asset-backed commercial paper ("ABCP").

### CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash in bank accounts and highly liquid money market instruments with maturities of three months or less from the date of acquisition, and are valued at cost, which approximates market value. Interest is earned at variable rates dependent on amount, credit quality and term.

### INVENTORIES

Inventories of logs, lumber, panels, pulp, kraft paper and chips are valued at the lower of average cost and net realizable value. Prior to January 1, 2008, logs were valued at average cost or the greater of net realizable value and replacement cost if lower than average cost (Note 2). Processing materials and supplies are valued at the lower of average cost and net realizable value.

### PROPERTY, PLANT, EQUIPMENT AND TIMBER

Canfor capitalizes the costs of major replacements, extensions and improvements to plant and equipment, together with related interest incurred during the construction period on major projects.

Assets are amortized over the following estimated productive lives:

| | |
|---|---|
| Buildings | 5 to 50 years |
| Mobile equipment | 5 years |
| Pulp and kraft paper machinery and equipment | 20 years |
| Sawmill machinery and equipment | 5 to 15 years |
| Plywood machinery and equipment | 5 to 15 years |
| Oriented strand board machinery and equipment | 10 to 20 years |
| Logging machinery and equipment | 4 to 20 years |
| Logging roads and bridges | 5 to 25 years |
| Timber – renewable licenses | 60 years |

Amortization of logging and manufacturing assets is calculated on a straight-line basis, based on available operating days, over the useful productive lives of those assets.

Amounts capitalized as timber, which comprise tree farm licenses and timber licenses that are renewable with the Province of British Columbia, are amortized over 60 years, effective January 1, 2008 (2007 – 100 years). Non-renewable licenses are amortized over the period of the license.

### LONG-LIVED ASSETS

Long-lived assets are reviewed for impairment when the occurrence of events or changes in circumstances indicate that the carrying value of the assets may not be recoverable, as measured by comparing their net book value to the estimated future cash flows generated by their use and eventual disposition. Impaired assets are recorded at the lower of carrying amount and fair value, determined principally using discounted future cash flows expected from their use and eventual disposition (see Note 20).

### GOODWILL

Goodwill is the excess of the purchase price paid for an acquisition of a business over the fair value of the net assets acquired. Goodwill is not amortized but is assessed annually for impairment, or more frequently if events or circumstances indicate that it may be impaired. The fair value of goodwill is estimated in the same manner as goodwill is determined at the time of acquisition. As at December 31, 2008, there were no write-downs to goodwill, all of which is denominated in US dollars.

### DEFERRED CHARGES

Software development costs relating to major systems are deferred and amortized over periods not longer than five years. Start-up costs for Canfor-LP OSB constructed in 2005 (Note 27) have been amortized over a three year period to December 31, 2008.

### DEFERRED REFORESTATION OBLIGATION

Forestry legislation in British Columbia requires Canfor to incur the cost of reforestation on its forest, timber and tree farm licenses. Accordingly, Canfor records the fair value of the costs of reforestation in the period in which the timber is cut, with the fair value of the liability determined with reference to the present value of estimated future cash flows using a credit adjusted risk free rate. In periods subsequent to the initial measurement, changes in the liability resulting from the passage of time and revisions to fair value calculations are recognized in the Consolidated Statements of Loss as they occur. These costs are included in manufacturing and product costs.

### ENVIRONMENTAL REMEDIATION COSTS

Costs associated with environmental remediation obligations are accrued and expensed when such costs are probable and can be reasonably estimated. Such accruals are adjusted as further information becomes available or circumstances change. Costs of future expenditures for environmental remediation obligations are discounted to their present value when the amount and timing of expected cash payments are reasonably determinable.

## ASSET RETIREMENT OBLIGATIONS

Canfor recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred when a reasonable estimate of fair value can be made and a legal obligation exists. The asset retirement costs equal to the fair value of the retirement obligations are capitalized as part of the cost of the related long-lived asset and allocated to amortization expense on a basis consistent with the expected useful life of the related asset. The liability is increased or accreted to full value with the passage of time based on the credit adjusted risk free interest rate with a periodic accretion expense charge to operating income. The liability is adjusted for any revisions to the timing or amount of the original estimate of undiscounted cash flows to discharge the liability.

## EMPLOYEE BENEFIT PLANS

Canfor has various defined benefit and defined contribution plans that provide both pension and other retirement benefits to most of its salaried employees and certain hourly employees not covered by forest industry union plans. Canfor also provides certain health care benefits and pension bridging benefits to eligible retired employees.

Canfor accrues the costs and related obligations of the defined benefit pension and other retirement benefit plans using the projected benefit actuarial method prorated on service, and management's best estimates of expected plan investment performance, salary escalation, and other relevant factors. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. Actuarial gains or losses arise from the difference between the actual and expected long-term rates of return on plan assets for a period or from changes in actuarial assumptions used to determine the accrued benefit obligation. The excess of the net accumulated actuarial gain or loss over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the average remaining service period of the active employees. Past service costs arising from plan amendments are deferred and amortized on a straight-line basis over the average remaining service period of employees active at the date of the amendment. On January 1, 2000, Canfor adopted the new recommendations of the Canadian Institute of Chartered Accountants relating to the accounting for pensions and other post employment benefits using the prospective application method. Canfor is amortizing the transitional balance on a straight-line basis over the average remaining service period of employees expected to receive benefits under the benefit plan as of January 1, 2000.

Pension expense for the defined contribution plans is based on a percentage of employees' salaries or on a contribution required under collective agreements.

For hourly employees covered by forest industry union defined benefit pension plans, the expense is equal to its contributions required under the collective agreements.

## REVENUE RECOGNITION

Canfor's revenues are derived from the following major product lines: lumber, pulp, kraft paper, panel products, residual fibre and logs. Revenue is recognized from product sales when persuasive evidence of a sale exists, the sales price is fixed and determinable, when title has transferred and collectability is reasonably assured. Sales are reported net of discounts, allowances and vendor rebates. Amounts charged to customers for shipping and handling are recognized as revenue, and shipping and handling costs incurred by Canfor are reported as a component of cost of sales. Lumber export taxes are recorded as a component of cost of sales.

## FOREIGN CURRENCY TRANSLATION

The majority of Canfor's sales and long-term debt are denominated in foreign currencies. Foreign currencies, except in respect of Canfor's foreign operations, are translated into Canadian dollars using the temporal method as follows: monetary assets and liabilities at year-end exchange rates; non-monetary assets and liabilities at historical rates; and revenues and expenses at exchange rates prevailing at the time the transaction occurs. Exchange gains and losses are reflected in income immediately.

Canfor's foreign operations are considered to be self-sustaining and the assets and liabilities are translated using the current rate method. The translation gain or loss is included as a component of accumulated other comprehensive income or loss in shareholders' equity.

### INCOME TAXES

Canfor accounts for income taxes using the liability method. Under this method, future income tax assets and liabilities are determined based on the temporary differences between the accounting basis and the tax basis of assets and liabilities. Those temporary differences are measured using the current tax rates and laws expected to apply when the differences reverse. Future tax benefits, such as capital loss carry-forwards, are recognized to the extent that realization of such benefits is considered more likely than not. The effect on future tax assets and liabilities of a change in income tax rates is recognized in earnings in the period that the substantive enactment date of the change occurs.

### DERIVATIVE FINANCIAL INSTRUMENTS

Canfor utilizes derivative financial instruments in the normal course of its operations as a means to manage its foreign exchange and commodity price risk. Canfor's policy is not to utilize derivative financial instruments for trading or speculative purposes.

Canfor has chosen to not designate its derivative financial instruments as hedges. Consequently, such derivatives for which hedge accounting is not applied are carried on the Consolidated Balance Sheets at fair value, with changes in (realized and unrealized) fair value being recognized as 'Gain (loss) on derivative financial instruments' in the Consolidated Statements of Loss.

### STOCK-BASED COMPENSATION PLANS

Canfor has three stock-based compensation plans, as described in Note 17. No stock options have been granted since 2002.

- Cash consideration received from employees when they exercise the options is credited to share capital.
- Compensation expense is recognized for Canfor's contributions to the Employee Share or Unit Purchase Plans when they are made.
- Compensation expense is recognized for Canfor's Deferred Share Unit Plans when the deferred share units are granted, and changes in market value of the underlying shares are reflected in earnings at the end of each period.

### MAJOR MAINTENANCE COSTS

CPLP has adopted the deferral method of accounting for major maintenance costs. Under this method an asset is recorded when expenditures related to major maintenance are incurred. This asset is then amortized over the period to which the maintenance relates. CPLP has presented the related unamortized expenditures in prepaid expenses and long-term investments and other, as appropriate.

## 2. CHANGES IN ACCOUNTING POLICIES

### CURRENT YEAR

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

#### (a) SECTION 1535 – CAPITAL DISCLOSURES

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

(b) SECTION 3031 – INVENTORIES

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

On January 1, 2008, Canfor adopted the new recommendations retrospectively, without prior period restatement. As a result of implementing these Standards, inventories decreased by $60.6 million (log inventories by $46.5 million, processing materials and supplies by $14.1 million), property, plant and equipment increased by $14.1 million, future income tax liabilities decreased by $15.9 million and opening retained earnings reduced by $30.6 million.

(c) SECTION 3862 – FINANCIAL INSTRUMENTS – DISCLOSURES

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

(d) SECTION 3863 – FINANCIAL INSTRUMENTS – PRESENTATION

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

## PRIOR YEAR

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

## FUTURE ACCOUNTING POLICY CHANGES

In February 2008, the CICA issued a new accounting standard, Handbook Section 3064 – "Goodwill and Intangible Assets". This Section replaces CICA Handbook Section 3062 – "Goodwill and Intangible Assets" and Section 3450 – "Research and Development Costs", and establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. On adoption of this new Standard, EIC 27 – "Revenues and Expenditures During the Pre-operating Period" is withdrawn and so various preproduction and start-up costs are required to be expensed as incurred. This Standard will be applicable to Canfor for annual and interim accounting periods beginning on January 1, 2009. Canfor does not expect that this Standard will have a material impact on its consolidated financial statements.

In 2008, the Canadian Accounting Standards Board announced that 2011 is the changeover date for publicly listed companies to use International Financial Reporting Standards ("IFRS"), replacing Canadian GAAP. The effective date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. From that date onwards, publicly traded companies and certain other publicly accountable enterprises will be required to report under IFRS. Canfor is currently evaluating the impact of these new standards on its consolidated financial statements.

## 3. ACQUISITIONS

### ACQUISITION OF DARLINGTON MILL

On November 30, 2007, Canfor completed the acquisition of the assets of Chesterfield Lumber Company, Inc., in Darlington, South Carolina ("Darlington mill"), through its wholly owned subsidiary, New South Companies, Inc., at a cost of US$18.8 million, including transaction costs. The sawmill has an annual capacity of approximately 140 million board feet of southern yellow pine lumber. The acquisition has been accounted for using the purchase method, in which the purchase consideration was allocated to the fair values of the assets and liabilities assumed on November 30, 2007. The purchase price allocation is summarized as follows:

| (millions of dollars) | | 2007 |
|---|---|---|
| Net assets acquired at November 30, 2007 | | |
| Non-cash working capital | $ | 3.0 |
| Property, plant and equipment | | 16.5 |
| Other liabilities | | (0.7) |
| Fair value of net assets acquired | $ | 18.8 |

## 4. ACCOUNTS RECEIVABLE

### TRADE RECEIVABLES

| (millions of dollars) | | **2008** | | 2007 |
|---|---|---|---|---|
| Gross receivables | $ | **108.9** | $ | 199.9 |
| Less: Allowance for doubtful accounts | | **(3.0)** | | (0.4) |
| | $ | **105.9** | $ | 199.5 |

### OTHER RECEIVABLES

(i) NORTH CENTRAL PLYWOODS MILL FIRE

Other receivables include $41.4 million in relation to a fire at Canfor's North Central Plywoods ("NCP") facility in Prince George, British Columbia on May 26, 2008, which completely destroyed the mill. The mill is insured for equivalent replacement value. At the end of the year, Canfor had not reached final settlement with its insurer, and accordingly estimated the insurance property damage amount receivable using preliminary engineering estimates and other information available. By December 31, 2008, Canfor had received advances of $30.0 million from the insurer which were offset against the total estimated property damage and business interruption receivable of $71.4 million. The insurance property damage receivable was estimated on the basis that the insurance proceeds will be applied towards capital improvements at Canfor's other operations.

Based on estimated insurance proceeds, net of an aggregate policy deductible and costs related to the fire, Canfor recorded a pre-tax gain of $57.9 million. The estimates are subject to adjustments in future periods.

(ii) PRINCE GEORGE PULP AND PAPER MILL FIRE

Other receivables include $7.2 million in relation to a fire at CPLP's Prince George Pulp & Paper mill in January 2008, which destroyed the chip screening and in-feed system. CPLP recorded a related pre-tax gain on disposal of capital assets of $8.2 million. In connection with claims arising from the fire, CPLP recorded the following receivables during 2008:

- a property damage insurance receivable of $12.2 million, net of a $3.3 million policy deductible; and
- a business interruption insurance receivable of $19.1 million, net of a $1.0 million policy deductible, plus a $3.0 million receivable for the temporary chip in-feed system costs.

By December 31, 2008, CPLP had received total advances of $27.1 million in connection with these claims, of which $15.9 million related to the business interruption claim, and $11.2 million to property damage. Of the latter amount, $9.5 million has been classified as an investing activity in the Consolidated Cash Flow Statements; the balance of $1.7 million represents demolition costs. Subsequent to December 31, 2008, a further $2.7 million has been received as partial payment against the accrued insurance receivable.

(iii) EXPORT TAX RECEIVABLE, NET

As at December 31, 2008, Canfor had a net export tax receivable of $3.3 million (2007 – payable of $5.2 million) as a result of a Third Country Adjustment export tax refund of $10.8 million related to the quarters ended December 31, 2007 and March 31, 2008. This refund was based on information received from the Canada Revenue Agency in December 2008.

## 5. INVENTORIES

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Logs (Note 2) | $ 49.1 | $ 105.9 |
| Lumber | 118.7 | 139.4 |
| Pulp | 97.2 | 71.2 |
| Paper | 20.7 | 14.1 |
| Panel products | 1.5 | 16.5 |
| Residual fibre | 25.3 | 11.2 |
| Processing materials and supplies (Note 2) | 92.4 | 113.7 |
| | $ 404.9 | $ 472.0 |

The above inventory balances are stated after inventory write-downs from cost to net realizable value, which reflect historically low prices for solid wood products in both years.

As a result of Canfor's implementation of Section 3031 – "Inventories" (Note 2), inventories on January 1, 2008 were decreased by $60.6 million (log inventories by $46.5 million and processing materials and supplies by $14.1 million).

Canfor's 2008 opening inventories, on which write-downs totaling $71.9 million were recorded ($25.4 million at December 31, 2007, plus the $46.5 million opening 2008 log inventories write-down adjustment), were consumed during 2008. Canfor's lower inventory write-downs of $46.2 million at December 31, 2008 resulted primarily from reduced costs and lower log volumes at year-end. As a result, the inventory write-downs at December 31, 2008 were $25.7 million less than at December 31, 2007.

The following table provides a breakdown of the inventory write-downs:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Logs (Note 2) | $ 16.2 | $ – |
| Lumber | 27.5 | 23.9 |
| Pulp | 2.1 | 0.2 |
| Panel products | 0.2 | 1.3 |
| Residual fibre | 0.2 | – |
| | $ 46.2 | $ 25.4 |

## 6. LONG-TERM INVESTMENTS AND OTHER

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Non-bank asset-backed commercial paper (Note 20) | $ 69.3 | $ 64.0 |
| Coastal Fibre Limited Partnership long-term fibre agreement (Note 20) | – | 37.1 |
| Other investments | 28.9 | 35.0 |
| Customer agreements | 22.9 | 21.1 |
| Derivative financial instruments | – | 4.4 |
| Other deposits, loans and advances | 4.6 | 8.8 |
| | $ 125.7 | $ 170.4 |

The non-bank asset-backed commercial paper of $69.3 million (US$56.6 million) is measured at the estimated fair value of Canfor's combined investments in asset-backed commercial paper of four different Canadian trusts with total original principal amount of US$81.2 million and original maturities between August and September 2007.

## 7. PROPERTY, PLANT, EQUIPMENT AND TIMBER

| (millions of dollars) | 2008 Cost | 2008 Accumulated Amortization & Impairments | 2008 Net Book Value | 2007 Cost | 2007 Accumulated Amortization & Impairments | 2007 Net Book Value |
|---|---|---|---|---|---|---|
| Land | $ 45.2 | $ 4.8 | $ 40.4 | $ 39.2 | $ 4.6 | $ 34.6 |
| Pulp and kraft paper mills | 1,323.6 | 751.9 | 571.7 | 1,303.1 | 719.4 | 583.7 |
| Sawmills, plywood and oriented strand board plants | 1,289.4 | 756.2 | 533.2 | 1,283.8 | 666.1 | 617.7 |
| Logging buildings and equipment | 12.4 | 4.8 | 7.6 | 12.7 | 4.0 | 8.7 |
| Logging roads and bridges | 150.1 | 140.3 | 9.8 | 150.0 | 127.5 | 22.5 |
| Other equipment and facilities | 28.5 | 15.0 | 13.5 | 35.5 | 15.7 | 19.8 |
| Timber | 838.8 | 216.5 | 622.3 | 838.8 | 166.4 | 672.4 |
| | $ 3,688.0 | $ 1,889.5 | $ 1,798.5 | $ 3,663.1 | $ 1,703.7 | $ 1,959.4 |

Included in the above costs are assets under construction in the amount of $11.0 million in 2008 (2007 – $10.0 million), which were not amortized.

## 8. DEFERRED CHARGES

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Prepaid pension benefits (Note 14) | $ 104.7 | $ 83.1 |
| Software development costs | 3.0 | 4.3 |
| Other | 2.5 | 2.6 |
| | $ 110.2 | $ 90.0 |

Deferred charges expensed during the year amounted to $4.7 million (2007 – $16.1 million).

## 9. OPERATING LOANS

At December 31, 2008, Canfor had $430.0 million of unsecured operating lines available (2007 – $409.0 million), of which $25.2 million was drawn down (2007 – nil) and $41.4 million was reserved for several standby letters of credit (2007 – $40.1 million).

Canfor Corporation's available operating line at December 31, 2008 was $355.0 million (2007 – $325.0 million) of which $17.3 million (2007 – $12.7 million) was reserved for several standby letters of credit, the majority of which relates to unregistered pension plans. Interest is payable at floating rates based on lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin that varies with Canfor's net debt to total capitalization ratio. The operating loan expires in June 2011.

CPLP's available operating line at December 31, 2008 was $75.0 million (2007 – $75.0 million) of which $25.2 million was drawn down (2007 – nil) and $24.1 million (2007 – $27.4 million) was reserved for a standby letter of credit issued to BC Hydro in connection with a 15 year electrical cogeneration agreement. Interest is payable at floating rates that vary depending on the ratio of net debt to operating earnings before interest, taxes, depreciation and amortization and is based on lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin. The operating loan expires in November 2009.

## 10. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Trade payables | $ 113.2 | $ 144.9 |
| Accrued payroll and related liabilities | 73.8 | 74.0 |
| Derivative financial instruments | 67.5 | 3.4 |
| Restructuring, mill closure and severance costs | 19.5 | 29.3 |
| Interest payable | 11.5 | 12.9 |
| Other | 37.4 | 70.5 |
| | $ 322.9 | $ 335.0 |

## 11. LONG–TERM DEBT

Canfor has the following long-term debt, all of which is unsecured:

### SUMMARY OF LONG-TERM DEBT

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Privately placed senior notes | | |
| Canfor Corporation | | |
| US $15 million, interest at 7.88%, repayable March 1, 2008 | $ – | $ 14.8 |
| US $45 million, interest at 7.98%, repayable March 1, 2009 | 55.1 | 44.5 |
| US $97 million, interest at 8.03%, repayable in 3 equal annual installments commencing March 1, 2009 | 118.8 | 95.9 |
| US $60 million, interest at 5.66%, repayable April 1, 2009 | 73.5 | 59.3 |
| US $50 million, interest at 6.18%, repayable April 1, 2011 | 61.2 | 49.4 |
| US $50 million, interest at 6.33%, repayable February 2, 2012 | 61.2 | 49.4 |
| US $75 million, interest at 5.42%, repayable April 1, 2013 | 91.9 | 74.1 |
| Canfor Pulp Limited Partnership | | |
| US $110 million, interest at 6.41%, repayable November 30, 2013 | 134.7 | 108.7 |
| Other long-term obligations | 0.6 | 0.7 |
| | 597.0 | 496.8 |
| Less: current portion | (168.3) | (15.2) |
| Long-term portion | $ 428.7 | $ 481.6 |

### FAIR VALUE OF TOTAL LONG-TERM DEBT

The fair value of total long-term debt at December 31, 2008 was $578.1 million (2007 – $502.2 million). The fair value was determined using prevailing market rates for long-term debt with similar characteristics and risk profiles.

### SCHEDULED LONG-TERM DEBT REPAYMENTS AND INTEREST PAYMENTS

Long-term debt repayments and interest payments for the next five years are as follows:

| (millions of dollars) | Debt Repayments | Interest Payments |
|---|---|---|
| 2009 | $ 168.3 | $ 33.5 |
| 2010 | 40.1 | 26.0 |
| 2011 | 100.8 | 21.0 |
| 2012 | 61.2 | 15.6 |
| 2013 | 226.6 | 10.4 |
| | $ 597.0 | $ 106.5 |

## 12. LONG-TERM ACCRUED LIABILITIES AND OBLIGATIONS

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Deferred reforestation obligation (Note 13) | $ 63.1 | $ 65.6 |
| Accrued pension obligations (Note 14) | 20.0 | 19.1 |
| Accrued pension bridge benefit obligations (Note 14) | 8.7 | 7.9 |
| Other post-employment benefits (Note 14) | 98.3 | 87.0 |
| Asset retirement obligations (Note 15) | 4.7 | 11.1 |
| Other | 14.0 | 12.8 |
| | $ 208.8 | $ 203.5 |

## 13. DEFERRED REFORESTATION OBLIGATION

Canfor's reforestation obligation and expense are as follows:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Reforestation obligation – beginning of year | $ 100.0 | $ 110.5 |
| Expense on current portion | 30.1 | 30.9 |
| Accretion expense | 3.6 | 3.3 |
| Changes in estimated future reforestation expenditures | (8.5) | (4.8) |
| Paid during the year | (29.6) | (39.9) |
| Reforestation obligation – end of year | $ 95.6 | $ 100.0 |
| Less: current portion | (32.5) | (34.4) |
| Long-term portion (Note 12) | $ 63.1 | $ 65.6 |

The total undiscounted amount of the estimated cash flows required to settle the obligation at December 31, 2008 was $105.7 million (2007 – $112.1 million) with payments spread over 18 years. The estimated cash flows have been adjusted for inflation and discounted using credit-adjusted risk-free rates ranging from 4% to 7%.

## 14. EMPLOYEE FUTURE BENEFITS

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

Total cash payments for employee future benefits for 2008 were $50.3 million (2007 – $61.2 million), consisting of cash contributed by Canfor to its funded pension plans, cash payments directly to beneficiaries for its unfunded other benefit plans, cash contributed to its defined contribution plans, and cash contributed to its forest industry union defined benefit plans.

### DEFINED BENEFIT PLANS

Canfor measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at September 30 of each year. In 2008, Canfor had seven registered defined benefit plans, for which actuarial valuations are performed every three years. The most recent actuarial valuation for funding purposes of Canfor's single largest pension plan was as of December 31, 2006, and the next required plan valuation is currently scheduled for December 31, 2009.

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

## DEFINED BENEFIT PLAN ASSETS

| (millions of dollars) | 2008 Pension Benefit Plans | 2008 Other Benefit Plans | 2007 Pension Benefit Plans | 2007 Other Benefit Plans |
|---|---|---|---|---|
| Fair market value of plan assets | | | | |
| Beginning of year | $ 571.1 | $ – | $ 517.8 | $ – |
| Actual (loss) gain on plan assets | (76.5) | – | 45.1 | – |
| Canfor contributions | 22.3 | 3.4 | 43.3 | 3.3 |
| Employee contributions | 1.1 | – | 1.4 | – |
| Benefit payments | (38.7) | (3.4) | (36.5) | (3.3) |
| Settlement of Taylor sawmill plan | (2.5) | – | – | – |
| End of year | $ 476.8 | $ – | $ 571.1 | $ – |

| | 2008 | 2007 |
|---|---|---|
| | Percentage of Plan Assets | |
| Plan assets consist of the following: | | |
| Asset Category | | |
| Equity securities | 61% | 64% |
| Debt securities | 38% | 33% |
| Real estate | 0% | 2% |
| Other | 1% | 1% |
| | 100% | 100% |

## DEFINED BENEFIT PLAN OBLIGATIONS

| (millions of dollars) | 2008 Pension Benefit Plans | 2008 Other Benefit Plans | 2007 Pension Benefit Plans | 2007 Other Benefit Plans |
|---|---|---|---|---|
| Accrued benefit obligation | | | | |
| Beginning of year | $ 570.2 | $ 146.7 | $ 581.4 | $ 139.2 |
| Current service cost | 13.3 | 2.6 | 16.3 | 3.5 |
| Interest cost | 31.2 | 8.1 | 30.2 | 7.4 |
| Employee contributions | 1.1 | – | 1.4 | – |
| Benefit payments | (38.7) | (3.4) | (36.5) | (3.3) |
| Settlement of Taylor sawmill plan | (2.5) | – | – | – |
| Special termination benefits | – | – | 2.1 | – |
| Actuarial gain | (64.0) | (50.4) | (24.7) | (0.1) |
| End of year | $ 510.6 | $ 103.6 | $ 570.2 | $ 146.7 |

RECONCILIATION OF THE FUNDED STATUS OF THE BENEFIT PLANS TO THE AMOUNTS RECORDED IN THE FINANCIAL STATEMENTS

| | 2008 | | 2007 | |
|---|---|---|---|---|
| (millions of dollars) | **Pension Benefit Plans** | **Other Benefit Plans** | Pension Benefit Plans | Other Benefit Plans |
| Fair market value of plan assets | $ 476.8 | $ – | $ 571.1 | $ – |
| Accrued benefit obligation | (510.6) | (103.6) | (570.2) | (146.7) |
| Funded status of plans – surplus (deficit) | (33.8) | (103.6) | 0.9 | (146.7) |
| Employer contributions after measurement date | 7.2 | 1.1 | 5.2 | 0.8 |
| Unamortized transitional amount | (17.5) | 13.9 | (21.2) | 15.9 |
| Unamortized past service costs | 3.0 | 1.2 | 3.4 | 1.3 |
| Unamortized net actuarial loss (gain) | 128.6 | (10.9) | 78.2 | 41.7 |
| Accrued benefit asset (liability) | 87.5 | (98.3) | 66.5 | (87.0) |
| Valuation allowance | (2.8) | – | (2.5) | – |
| Accrued benefit asset (liability), net of valuation allowance | $ 84.7 | $ (98.3) | $ 64.0 | $ (87.0) |
| The accrued benefit asset (liability) is included in Canfor's balance sheet as follows: | | | | |
| Deferred charges (Note 8) | $ 104.7 | $ – | $ 83.1 | $ – |
| Long-term accrued liabilities and obligations (Note 12) | (20.0) | (98.3) | (19.1) | (87.0) |
| | $ 84.7 | $ (98.3) | $ 64.0 | $ (87.0) |

Excluded from the above tables are amounts relating to a defined benefit pension plan of New South Companies, Inc., which was curtailed in 2003. The accrued benefit asset at December 31, 2008 was $0.3 million (2007 – $0.3 million).

Included in the above pension and other benefit provisions and fair value of plan assets at year-end are the following amounts in respect of plans that are not fully funded:

| | 2008 | | 2007 | |
|---|---|---|---|---|
| (millions of dollars) | **Pension Benefit Plans** | **Other Benefit Plans** | Pension Benefit Plans | Other Benefit Plans |
| Fair market value of plan assets | $ 395.2 | $ – | $ 67.9 | $ – |
| Accrued benefit obligation | (440.2) | (103.6) | (97.0) | (146.7) |
| Funded status – plan deficit | $ (45.0) | $ (103.6) | $ (29.1) | $ (146.7) |

Of the $45.0 million of pension plan deficit at December 31, 2008, $25.1 million relates to unregistered plans for which funding is not required (2007 – $27.1 million). Unregistered pension liabilities at December 31, 2008 include $12.7 million (2007 – $9.5 million), which are secured by a letter of credit.

"Other benefit plans" are not funded, except when expenditures are incurred.

Canfor's expense for company-sponsored benefit plans is as follows:

| (millions of dollars) | 2008 Incurred in Year | 2008 Matching Adjustments[a] | 2008 Recognized in Year | 2007 Incurred in Year | 2007 Matching Adjustments[a] | 2007 Recognized in Year |
|---|---|---|---|---|---|---|
| **Pension Benefit Plans** | | | | | | |
| Current service cost | $ 13.3 | $ – | $ 13.3 | $ 16.3 | $ – | $ 16.3 |
| Interest cost | 31.2 | – | 31.2 | 30.2 | – | 30.2 |
| Loss (return) on plan assets | 76.5 | (117.4) | (40.9) | (45.1) | 9.7 | (35.4) |
| Actuarial (gain) loss | (64.0) | 67.0 | 3.0 | (24.7) | 32.0 | 7.3 |
| Special termination benefits | – | – | – | 2.1 | – | 2.1 |
| Settlement/Curtailment loss | 0.3 | – | 0.3 | – | – | – |
| Plan amendments | – | 0.4 | 0.4 | – | 0.4 | 0.4 |
| Valuation allowance provided against accrued benefit asset | – | 0.3 | 0.3 | – | 0.3 | 0.3 |
| Amortization of transitional asset | – | (3.7) | (3.7) | – | (3.7) | (3.7) |
| | $ 57.3 | $ (53.4) | $ 3.9 | $ (21.2) | $ 38.7 | $ 17.5 |
| **Other Benefit Plans** | | | | | | |
| Current service cost | $ 2.6 | $ – | $ 2.6 | $ 3.5 | $ – | $ 3.5 |
| Interest cost | 8.1 | – | 8.1 | 7.4 | – | 7.4 |
| Actuarial loss (gain) | (50.4) | 52.6 | 2.2 | (0.1) | 2.3 | 2.2 |
| Plan amendments | – | 0.1 | 0.1 | – | 0.1 | 0.1 |
| Amortization of transitional obligation | – | 2.0 | 2.0 | – | 2.0 | 2.0 |
| | $ (39.7) | $ 54.7 | $ 15.0 | $ 10.8 | $ 4.4 | $ 15.2 |

(a) Matching adjustments are accounting adjustments to allocate costs to different periods so as to recognize the long-term nature of employee future benefits.

Canfor also provides pension bridge benefits to certain eligible former employees. At December 31, 2008, the actuarially determined obligation for those benefits was $15.4 million (2007 – $17.7 million). The accrued benefit liability for those benefits at December 31, 2008 was $8.7 million (2007 – $7.9 million) (Note 12) and the related expense recognized in 2008 was $2.2 million (2007 – $2.0 million).

## SIGNIFICANT ASSUMPTIONS

The actuarial assumptions used in measuring Canfor's benefit plan provisions are as follows:

| (weighted average assumptions) | 2008 Pension Benefit Plans | 2008 Other Benefit Plans | 2007 Pension Benefit Plans | 2007 Other Benefit Plans |
|---|---|---|---|---|
| Accrued benefit obligation as of December 31: | | | | |
| Discount rate | 6.60% | 6.70% | 5.60% | 5.50% |
| Rate of compensation increase | 3.00% | n/a | 3.00% | n/a |
| Benefit costs for year ended December 31: | | | | |
| Discount rate | 5.60% | 5.50% | 5.25% | 5.25% |
| Expected long-term rate of return on plan assets | 7.50% | n/a | 7.00% | n/a |
| Rate of compensation increase | 3.00% | n/a | 3.00% | n/a |

## ASSUMED HEALTH CARE COST TREND RATES

| (weighted average assumptions) | 2008 | 2007 |
|---|---|---|
| Initial health care cost trend rate | 5.83% | 5.62% |
| Ultimate health care trend rate | 4.40% | 4.27% |
| Year ultimate rate is reached | 2014 | 2011 |

SENSITIVITY ANALYSIS

Assumed health care cost trend rates have a significant effect on the amounts reported for the other benefit plans. A one percentage-point change in assumed health care cost trend rates would have the following effects for 2008:

| | 1% Increase | 1% Decrease |
|---|---|---|
| Accrued benefit obligation | $ 16.7 | $ (13.6) |
| Total of service and interest cost | $ 2.3 | $ (1.8) |

### DEFINED CONTRIBUTION AND OTHER PLANS

The total cost recognized in 2008 for Canfor's defined contribution plans was $3.6 million (2007 – $1.6 million).

Canfor contributes to various forest industry union defined benefit pension plans providing both pension and other retirement benefits. These plans are accounted for as defined contribution plans. Contributions to these plans, not included in the cost recognized for defined contribution plans above, amounted to $17.4 million in 2008 (2007 – $20.9 million).

## 15. ASSET RETIREMENT OBLIGATIONS

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Balance, beginning of year | $ 13.2 | $ – |
| Accrued obligation | – | 13.4 |
| Accretion expense | 0.4 | 0.1 |
| Paid during the year | (1.2) | (0.3) |
| Gain on settlement | (0.9) | – |
| Change in estimate | (6.8) | – |
| Balance, end of year | $ 4.7 | $ 13.2 |
| Less: current portion | – | (2.1) |
| Long-term portion (Note 12) | $ 4.7 | $ 11.1 |

In 2008, CPLP completed remediation of an ash pond at its Intercontinental pulp mill. In 2007, CPLP recorded an obligation based on the fair value of the containment estimate of $2.4 million, with a corresponding capital addition to the related asset. The final costs to remediate the ash pond were $1.5 million and as a result, CPLP recognized a gain of $0.9 million on settlement of the ash pond, which is included in 'Other Income' on the 2008 Consolidated Statement of Loss.

Following a review in 2008 of the useful lives and landfill closure costs, CPLP reduced its asset retirement obligations and the related asset by $6.8 million. CPLP's obligations as at December 31, 2008 reflect estimated undiscounted future payments of $20.3 million. The future payments relating to landfill closure costs are discounted at 5.8% and 6.3% and are expected to occur at periods ranging from 32 to 40 years.

Canfor has certain assets that have indeterminable useful lives 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. Once the useful life of these assets becomes determinable and an estimate of fair value can be made, an asset retirement obligation will be recorded.

It is possible that changes in future conditions in the near term could require a material change in the recognized amount of the asset retirement obligations.

## 16. SHARE CAPITAL

### AUTHORIZED

10,000,000 preferred shares, with a par value of $25 each

1,000,000,000 common shares without par value

| (millions of dollars) | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|
| | Number of Shares | | Amount | Number of Shares | | Amount |
| Common shares, beginning of year | 142,589,312 | $ | 1,124.7 | 142,548,812 | $ | 1,124.3 |
| Stock options exercised (Note 17) | – | | – | 40,500 | | 0.4 |
| Common shares, end of year | 142,589,312 | $ | 1,124.7 | 142,589,312 | $ | 1,124.7 |

## 17. STOCK-BASED COMPENSATION

Canfor has three stock-based compensation plans, which are described below.

### STOCK OPTION PERFORMANCE PLAN

The Company has a stock option performance plan pursuant to which stock options were granted to selected officers and senior managers. No new stock options were granted in 2008 or 2007. The stock option performance plan provided for the issuance of up to a maximum of 5.8 million common shares at an exercise price equal to the market price of the Company's common shares on the date of grant. However, there are various criteria that limit the amount of options exercisable during each option year within the option period. The options are for a term of ten years and vest equally over three years. All options have fully vested. A summary of the status of the plan as of December 31, 2008 and 2007, and changes during the years ending on those dates, is presented below:

| | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|
| | Number of Shares | | Weighted Average Exercise Price | Number of Shares | | Weighted Average Exercise Price |
| Outstanding at the beginning of year | 213,801 | $ | 9.39 | 261,969 | $ | 9.29 |
| Exercised | – | | – | (40,500) | | 8.82 |
| Expired | (13,333) | | 10.18 | (7,668) | | 9.12 |
| Outstanding at the end of the year | 200,468 | $ | 9.34 | 213,801 | $ | 9.39 |

The following table summarizes information about stock options outstanding at December 31, 2008:

| | Options outstanding | | | | Options exercisable | | |
|---|---|---|---|---|---|---|---|
| Range of exercise prices | Number of Options Outstanding | Weighted Average Remaining Life (years) | | Weighted Average Exercise Price | Number of Options Exercisable | | Weighted Average Exercise Price |
| $8.30 | 63,800 | 2.1 | $ | 8.30 | 63,800 | $ | 8.30 |
| $9.80 to $11.80 | 136,668 | 3.1 | | 9.82 | 136,668 | | 9.82 |
| | 200,468 | 2.8 | $ | 9.34 | 200,468 | $ | 9.34 |

## EMPLOYEE SHARE AND UNIT PURCHASE PLANS

The Company has a share purchase plan, which is available to all employees, other than CPLP employees. Purchases of common shares under this plan occur on the open market. Under the plan, employees can purchase up to 10% of their base salary or wage. Up to June 2007, the Company matched 30% of the first 5% of the amount contributed by the employee and paid the plan's brokerage fees. Since July 2007, the Company has not made any contributions towards the purchase of its shares under the plan (2007 – $0.6 million).

CPLP has a unit purchase plan, which is available to all CPLP employees. Purchases of Canfor Pulp Income Fund units under this plan occur on the open market. Under the plan the employees can purchase up to 10% of their base salary or wage. CPLP matches 30% of the first 5% of the amount contributed by the employee and pays the plan's brokerage fees. In 2008, CPLP made contributions of $0.6 million towards the purchase of the units of Canfor Pulp Income Fund under the plan (2007 – $0.5 million).

## DEFERRED SHARE UNIT PLANS

On January 1, 2002, the Company implemented a Deferred Share Unit Plan for non-employee directors of the Company. A Deferred Share Unit ("DSU") is a right granted to a non-employee director to receive one common share of the Company, purchased on the open market, or the cash equivalent, on a deferred payment basis. The maximum number of DSUs outstanding under the plan is 1,000,000, and currently each non-employee director is entitled to 2,500 DSUs per year. The value of the DSUs, when redeemed, is equal to the market value of the shares on the redemption date, including the value of dividends paid on the Company's common shares, if any, as if they had been reinvested in additional DSUs on each payment date. The DSUs may only be redeemed upon a director's retirement from the Company, its subsidiaries or any affiliated entity. The value of the outstanding DSUs at December 31, 2008 was $0.7 million (2007 – $0.7 million).

In May 2007, the Company implemented a Deferred Share Unit Plan for the Company's CEO (the "CEO Plan"). Pursuant to the terms of the plan, the CEO receives his annual salary in DSU units, which are allocated on a monthly basis. The value of the DSUs when redeemed will be equal to the market value of the shares on the redemption date, including the value of dividends paid on the Company's common shares, if any, as if they had been reinvested in additional DSUs on each payment date. The DSUs under the CEO Plan may only be redeemed on the date the CEO ceases, for whatever reason, to be employed by the Company. The value of the outstanding CEO DSUs at December 31, 2008 was $0.7 million (2007 – $0.3 million).

# 18. RESTRUCTURING, MILL CLOSURE AND SEVERANCE COSTS

Restructuring, mill closure and severance costs represent costs associated with the indefinite or permanent closures of facilities and staff reductions. The expense for the year ended December 31, 2008 amounted to $53.5 million (2007 – $41.3 million) and substantially resulted from the indefinite closures of the Mackenzie sawmill and PolarBoard and Tackama panel operations, as well as the permanent closure of the NCP plywood operation following a fire that destroyed the plant (Note 4(i)).

The following table provides a breakdown of the restructuring, mill closure and severance costs by business segment:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Lumber | $ 18.7 | $ 21.7 |
| Panels | 34.5 | 14.4 |
| Corporate and Other | 0.3 | 5.2 |
| | $ 53.5 | $ 41.3 |

The following table provides a reconciliation of the restructuring, mill closure and severance liability for the 2007 and 2008 years:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Accrued liability at beginning of year | $ 29.8 | $ 4.9 |
| Costs in the period[a] | 39.8 | 33.3 |
| Paid during the year | (46.3) | (8.4) |
| Accrued liability at end of year | $ 23.3 | $ 29.8 |

(a) Excluding non-cash expenses, which include provisions for capital asset and inventory write-downs resulting from indefinite and permanent mill closures, in both years.

## 19. INTEREST INCOME (EXPENSE)

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Interest expense | $ (38.7) | $ (44.1) |
| Less: Interest income | 13.3 | 34.7 |
| Interest expense, net | $ (25.4) | $ (9.4) |

Interest expense, net is comprised of:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Short-term interest income, net | $ 9.5 | $ 28.3 |
| Long-term interest expense, net | (34.9) | (37.7) |
| Interest expense, net | $ (25.4) | $ (9.4) |

For the year ended December 31, 2008, short-term interest income, net is comprised of interest income of $13.2 million on cash and cash equivalents (2007 – $34.6 million), less interest expense of $3.7 million on loans and letter of credit charges (2007 – $6.3 million). The 2008 long-term interest expense, net is comprised of interest expense of $35.0 million on long-term debt (2007 – $37.8 million), less interest income of $0.1 million on long-term advances (2007 – $0.1 million).

## 20. ASSET IMPAIRMENTS

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Capital assets | $ 77.2 | $ 231.4 |
| Assets related to Howe Sound Pulp and Paper Limited Partnership and Coastal Fibre Limited Partnership | 70.0 | 14.0 |
| Non-bank asset-backed commercial paper (Note 6) | 10.2 | 16.2 |
| Other | 12.2 | 6.4 |
| | $ 169.6 | $ 268.0 |

### CAPITAL ASSETS

Canfor reviews the carrying values of its long-lived assets on a regular basis as events or changes in circumstances may warrant. Where the carrying value of assets is not expected to be recoverable from future cash flows, they are written down to fair value. A review of the carrying values of Canfor's sawmill and panelboard operations and various other assets was undertaken in 2007 and 2008 as a result of operating losses in both years and the difficult market conditions.

The first step in this process was to determine for each operation whether projected undiscounted future cash flows from operations exceeded the net carrying amount of the assets as of the assessment date. For those operations where an impairment was indicated, the second step was to calculate fair values using discounted future cash flows expected from their use and eventual disposition.

Estimates of future cash flows used to test the recoverability of Canfor's long-lived assets generally include key assumptions related to forecast prices and exchange rates. Other significant assumptions are the estimated useful life of the long-lived assets, and the impacts of both the Softwood Lumber Agreement with the U.S. and the Mountain Pine Beetle epidemic. Price forecasts beyond 2009 were determined with reference to Resource Information Systems, Inc. publications, and forecast exchange rates were based on forecasts from various recognized authorities. Given the importance of the US$/Cdn$ exchange rate in Canfor's business, where most sales are denominated in US dollars and most costs incurred in Canadian dollars, probabilities were assigned to the likelihood of occurrence of several exchange rate scenarios, and a weighted average of these was used in determining the impairments to be recorded.

As a result of its review, Canfor recorded a capital asset impairment charge of $77.2 million (2007 – $231.4 million).

### ASSETS RELATED TO HOWE SOUND PULP AND PAPER LIMITED PARTNERSHIP AND COASTAL FIBRE LIMITED PARTNERSHIP

For the year ended December 31, 2008, an asset impairment charge of $70.0 million (2007 – $14.0 million) was recorded for assets related to Howe Sound Pulp and Paper Limited Partnership ("HSLP"), which reflects fair value based on estimated future cash flows. Canfor's investments include a 50% interest in Coastal Fibre Limited Partnership ("CFLP"), an entity which supplies chips and logs and related services to HSLP. The impairment reflects the deterioration of BC Coastal pulp, paper and fibre market conditions (Notes 26 and 27).

### NON-BANK ASSET-BACKED COMMERCIAL PAPER

Since August 2007, there has been no active market for non-bank asset-backed commercial paper ("ABCP"). Canfor's funds are invested in the ABCP of four different Canadian trusts, which failed to make payment at maturity and, along with 16 other ABCP conduits, were subject to restructuring under the Pan-Canadian Investors Committee for Third Party structured Asset-Backed Commercial Paper ("the Pan-Canadian Investors Committee"). On March 17, 2008 the Pan-Canadian Investors Committee filed with the Ontario Superior Court of Justice a comprehensive arrangement pursuant to the Companies' Creditors Arrangement Act to restructure the affected trusts. The final restructuring plan was approved on January 12, 2009 and completed on January 21, 2009.

At December 31, 2008 an additional impairment of $10.2 million (US$8.4 million) was recorded on the ABCP based on the estimated fair value at year end, which took into account information available to Canfor related to its specific holdings of ABCP, and assumed a high likelihood of success for the ABCP restructuring plan. The book value at December 31, 2008 reflected the impact of a weaker Canadian dollar on the US dollar denominated ABCP. No changes to fair value resulted from the completion of the restructuring plan after year-end 2008.

### OTHER

For the year ended December 31, 2008, other asset impairments of $12.2 million were recognized for certain other investments and spare parts inventory at indefinitely idled operations.

## 21. OTHER INCOME (EXPENSE)

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Foreign exchange gain (loss) on translation of working capital | $ 17.3 | $ (14.1) |
| Dividend income | – | 5.0 |
| Other, net | (4.6) | (2.0) |
| | $ 12.7 | $ (11.1) |

## 22. INCOME TAXES

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

| | 2008 | | 2007 | |
|---|---|---|---|---|
| (millions of dollars) | Current | Long-term | Current | Long-term |
| Future income tax assets | | | | |
| Accruals not currently deductible | $ 23.2 | $ 22.9 | $ 23.7 | $ 24.1 |
| Derivative financial instruments | 21.2 | 1.0 | – | – |
| Non-capital loss carryforwards | – | 18.4 | – | 7.3 |
| Investments | 0.2 | 2.5 | – | 3.4 |
| Post employment benefits | – | 27.5 | – | 25.8 |
| Other | 0.2 | 8.4 | 0.4 | 1.4 |
| | $ 44.8 | $ 80.7 | $ 24.1 | $ 62.0 |
| Future income tax liabilities | | | | |
| Depreciable capital assets | $ – | $ (270.8) | $ – | $ (305.7 ) |
| Deferred pension and other costs | – | (33.2) | – | (28.0) |
| Unrealized foreign exchange gains on debt | – | (7.1) | – | (23.8) |
| Income from limited partnerships | (13.2) | – | (21.8) | – |
| Derivative financial instruments | – | – | (5.6) | (0.9) |
| Other | (0.4) | (12.0) | (15.7) | (3.1) |
| | $ (13.6) | $ (323.1) | $ (43.1) | $ (361.5) |
| Future income taxes, net | $ 31.2 | $ (242.4) | $ (19.0) | $ (299.5) |

The components of income tax recovery are as follows:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Current | $ 47.9 | $ 140.8 |
| Future | 94.0 | 93.3 |
| | $ 141.9 | $ 234.1 |

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

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Net loss before income taxes and non-controlling interests | $ (463.1) | $ (529.3) |
| Income tax recovery at statutory tax rate | $ 143.6 | $ 180.5 |
| Add (deduct): | | |
| Non-controlling interests | 7.4 | 22.3 |
| Change in corporate income tax rates | 9.1 | 21.5 |
| Entities with different income tax rates and other tax adjustments | 4.4 | 12.4 |
| Tax recovery at rates other than statutory rate | 3.5 | – |
| Permanent difference from capital gains and losses and other non-deductible items | (26.1) | (2.6) |
| Income tax recovery | $ 141.9 | $ 234.1 |

## 23. NET LOSS PER SHARE

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

| | 2008 | 2007 |
|---|---|---|
| Weighted average number of common shares | 142,589,312 | 142,576,271 |
| Incremental shares from potential exercise of stock options[a] | 1,778 | 41,254 |
| Diluted number of common shares[a] | 142,589,312 | 142,576,271 |

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

## 24. NET CHANGE IN NON-CASH WORKING CAPITAL

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Accounts receivable | $ 78.1 | $ 38.0 |
| Income taxes recoverable/payable | 89.6 | (371.9) |
| Future income taxes, net | (49.9) | 14.0 |
| Inventories | 2.9 | 166.8 |
| Prepaid expenses | (0.1) | 1.9 |
| Accounts payable, accrued liabilities and current portion of deferred reforestation obligation | (64.4) | (277.3) |
| | $ 56.2 | $ (428.5) |

## 25. FINANCIAL INSTRUMENTS

All financial instruments and derivatives are measured at fair value on initial recognition except for certain related party transactions. Unless otherwise stated, book value approximates fair value.

### CLASSIFICATION OF FINANCIAL INSTRUMENTS

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

Canfor reviews all assets, including financial instruments, for impairment when events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable.

### FINANCIAL RISK MANAGEMENT

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

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

### (a) CREDIT RISK:

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

Financial instruments that are subject to credit risk include cash and cash equivalents, accounts receivable and long-term investments and other. Cash and cash equivalents includes cash held through major Canadian and international financial institutions and temporary investments with an original maturity date of three months or less. The cash and cash equivalents balance at December 31, 2008 is $362.4 million.

Canfor utilizes a combination of credit insurance and self-insurance to manage the risk associated with trade receivables. Approximately 50% of the outstanding trade receivables are covered by credit insurance. Canfor's trade receivable balance at December 31, 2008 is $105.9 million, net of an allowance for doubtful accounts of $3.0 million. At December 31, 2008, approximately 98% of the trade accounts balance was within Canfor's established credit terms.

### (b) LIQUIDITY RISK:

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

At December 31, 2008, Canfor has operating loans of $25.2 million, accounts payable and accrued liabilities of $322.9 million and current debt obligations of $168.3 million (US$137.3 million), all of which fall due for payment within one year of the balance sheet date.

### (c) 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 and commodity prices.

#### (i) INTEREST RATE RISK:

Canfor is exposed to interest rate risk through its current financial assets and financial obligations bearing variable interest rates. Canfor's cash and cash equivalents include term deposits with original maturity dates of three months or less.

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

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

#### (ii) CURRENCY RISK:

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

An increase (decrease) in the value of the Canadian dollar by US$0.01 would result in a pre-tax: (i) 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); (ii) loss (gain) of approximately $0.8 million in relation to the ABCP denominated in US dollars at year end; (iii) gain (loss) of approximately $6.4 million in relation to long-term debt denominated in US dollars at year end 2008.

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

Canfor had the following foreign exchange derivatives at December 31, 2008 and 2007:

| | 2008 | | | | 2007 | | | |
|---|---|---|---|---|---|---|---|---|
| | Notional Amount | | Average Rate | | Notional Amount | | Average Rate | |
| **US dollars** | | (millions of US dollars) | | (per dollar) | | (millions of US dollars) | | (per dollar) |
| 0 – 12 months | | | | | | | | |
| US Dollar Collars | $ | 397.0 | | $0.9800 – $1.1328 | $ | 404.0 | $ | 1.00 – $1.1275 |
| US Dollar Forward Contracts | $ | 95.8 | | $ 1.1963 – $1.2618 | $ | 8.7 | $ | 0.9981 |
| 13 – 24 months | | | | | | | | |
| US Dollar Collars | | – | | – | $ | 64.0 | $ | 1.00 – $1.1206 |

An increase (decrease) in the value of the Canadian dollar by US$0.01 would result in a pre-tax gain (loss) of approximately $5 million in relation to the foreign exchange collars and forward contracts held at year end.

#### (iii) ENERGY PRICE RISK:

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

The exposure is hedged up to 100% through the use of floating to fixed swap contracts or option contracts with maturity dates up to a maximum of three years. In the case of diesel, Canfor uses heating oil contracts to hedge its exposure.

Canfor had the following energy derivatives at December 31, 2008 and 2007:

| | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|
| | Notional Amount | Average Price | | Notional Amount | Average Price | |
| **Natural gas** | (millions of gigajoules) | | (dollars per gigajoule) | (millions of gigajoules) | | (dollars per gigajoule) |
| Floating to Fixed Swap | | | | | | |
| 0 – 12 Months | 4.2 | $ | 7.58 | 4.8 | $ | 7.25 |
| 13 – 36 Months | 2.7 | $ | 7.76 | 5.3 | $ | 7.61 |
| **Diesel** | (millions of gallons) | | (dollars per gallon) | (millions of gallons) | | (dollars per gallon) |
| Floating to Fixed Swap | | | | | | |
| 0 – 12 Months | 5.3 | $ | 2.76 | 9.8 | $ | 1.97 |
| 13 – 36 Months | 1.2 | $ | 2.70 | 3.5 | $ | 1.82 |
| Call Option | | | | | | |
| 0 – 12 Months | 3.0 | $ | 3.55 | – | | – |

An increase (decrease) in the market price of natural gas of $0.10 per gigajoule would result in a pre-tax gain (loss) of approximately $0.7 million in relation to the natural gas swaps held at year end.

An increase (decrease) in the market price of diesel of $0.10 per gallon would result in a pre-tax gain (loss) of approximately $0.7 million in relation to the diesel swaps held at year end.

#### (iv) COMMODITY PRICE RISK:

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

Canfor had no futures contracts at December 31, 2008.

| | 2008 | | 2007 | | |
|---|---|---|---|---|---|
| | **Notional Amount** | **Average Rate** | Notional Amount | Average Rate | |
| **Lumber** | (MMfbm) | (dollars per Mfbm) | (MMfbm) | | (dollars per Mfbm) |
| Futures Contracts 0 – 12 months | – | – | 34.1 | $ | 281.62 |

## DERIVATIVE INSTRUMENTS

Canfor uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, lumber prices and energy costs. At December 31, 2008, the fair value of outstanding commodity and exchange financial instruments was a net liability of $69.3 million (2007 – net asset of $17.2 million). 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 years ended December 31, 2008 and 2007:

| (millions of dollars) | | 2008 | | 2007 |
|---|---|---|---|---|
| Foreign exchange collars and forward contracts | $ | (86.1) | $ | 14.3 |
| Natural gas swaps | | (0.4) | | (4.0) |
| Diesel options and swaps | | (3.4) | | 9.1 |
| Commodity futures | | – | | 1.7 |
| | $ | (89.9) | $ | 21.1 |
| Reclassification to income of gains (losses) on derivatives designated as cash flow hedges in prior periods[a] | | 1.4 | | (5.1) |
| (Loss) gain on derivative financial instruments | $ | (88.5) | $ | 16.0 |

(a) Net of taxes and non-controlling interests

The following table summarizes the fair market value of the derivative financial instruments included in the balance sheet at December 31, 2008 and 2007:

| (millions of dollars) | | 2008 | | 2007 |
|---|---|---|---|---|
| Foreign exchange collars and forward contracts | $ | (53.2) | $ | 15.0 |
| Natural gas swaps | | (6.5) | | (5.7) |
| Diesel options and swaps | | (9.6) | | 7.9 |
| | | (69.3) | | 17.2 |
| Less: current portion | | (67.5) | | 14.4 |
| Long-term portion | $ | (1.8) | $ | 2.8 |

## 26. RELATED PARTY TRANSACTIONS

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

### HOWE SOUND PULP AND PAPER LIMITED PARTNERSHIP

Howe Sound Pulp and Paper Limited Partnership ("HSLP") is jointly owned by Canfor and Oji Paper Co. Ltd. ("Oji") and operates a kraft pulp and newsprint mill at Port Mellon, British Columbia. Canfor has the following related party transactions with HSLP:

(a) Under a long-term fibre agreement with Western Forest Products Inc., CFLP purchases chips and logs for resale to HSLP at CFLP's cost. In 2008, these purchases totaled $18.5 million and $21.8 million respectively (2007 – $15.8 million, $18.8 million) and the balance receivable at December 31, 2008 was $19.1 million (2007 – $15.8 million). CFLP charges HSLP a commission for this service, which amounted to $0.3 million in 2008 (2007 – $0.2 million). There was a balance receivable of $0.8 million at December 31, 2008 (2007 – $0.5 million). These amounts have been proportionately consolidated in Canfor's financial statements.

(b) Canfor and Oji, the partners of HSLP, and HSLP have a prepayment agreement whereby the partners prepay HSLP in advance of the due date for receivables for pulp marketed, or to be marketed, and collected on their behalf. Canfor charges a market rate of interest to HSLP for the period paid in advance and the prepayment is partially covered by the assignment of current or future accounts receivable. The agreement provides for Oji to prepay up to a maximum amount of $60.0 million and Canfor to a maximum of $50.0 million, which is used as short-term operating funds by HSLP. In addition, Canfor has granted extended credit terms to HSLP up to a maximum of $10.0 million. Canfor, through CPLP, markets the pulp production of HSLP for which it receives commissions under the terms of its agency sales agreement. Canfor provides management, fibre supply and other services to HSLP at cost. At December 31, 2008, Canfor has a balance of $31.4 million owing from HSLP (2007 – $32.8 million).

(c) As a consequence of a debt restructuring agreement among HSLP, Canfor, Oji and a consortium of Japanese banks (the "Banks") in February 2008, Canfor contributed additional funds to HSLP of $18.8 million, which were still outstanding at year end. These funds are secured by the assets of HSLP, subject to other security granted to the Banks and Oji. The repayment of these funds has priority over all other repayments, except a minimum bank debt repayment, from the annual free cash flow of HSLP.

The transactions with HSLP in 2008 and 2007 are summarized below:

| (millions of dollars) | 2008 | 2007 |
|---|---|---|
| Chips purchased for resale to HSLP | $ 9.3 | $ 7.9 |
| Pulp logs purchased for resale to HSLP | 10.9 | 9.4 |
| Interest | 3.1 | 2.8 |
| Commission earned from marketing of HSLP pulp | 2.6 | 2.9 |
| Other | 0.3 | 0.7 |
| | $ 26.2 | $ 23.7 |

As at December 31, 2008, Canfor has recorded a net amount receivable from HSLP of $11.3 million (2007 – $26.1 million).

### OTHER RELATED PARTIES

Canfor purchases chips and lumber from Lakeland Mills Ltd. and Winton Global Lumber Ltd., in which Canfor has a 33.3% interest. In 2008, Canfor purchased $6.0 million in chips and $1.5 million in lumber (2007 – $11.5 million and $8.7 million respectively). The balance outstanding at December 31, 2008 was $0.2 million (2007 – $0.6 million).

Kyahwood Forest Products Ltd. ("Kyahwood"), in which Canfor had an interest until April 2008 when it disposed of its investment, provided remanufacturing services to Canfor totaling $4.2 million in 2007. There were no transactions in 2008.

In 2008, shipping services provided by Seaboard International Shipping Company ("Seaboard"), in which Canfor has a 20% interest, amounted to $3.4 million (2007 – $5.3 million). There was no balance outstanding at December 31, 2008 (2007 – $0.3 million). On December 29, 2008 Canfor received a loan of $2.9 million from the Seaboard General Partnership, which owns Seaboard, by way of a demand, non-interest bearing promissory note payable on or before January 2, 2009. On January 2, 2009, Seaboard General Partnership declared an income distribution to its partners of which Canfor's share was $2.9 million. The distribution was received by way of offset against the non-interest bearing promissory note of the same amount.

Louisiana-Pacific Canada Ltd. performs the sales and receivable functions for Peace Valley OSB, an oriented strand board mill located in Fort St. John, British Columbia (Note 27). In 2008, Louisiana-Pacific Canada Ltd. sold $110.7 million of Peace Valley OSB inventory (2007 – $112.9 million). Louisiana-Pacific Canada Ltd. charges a fee for this service, which amounted to $3.1 million in 2008 (2007 – $1.8 million). There was a net payable to Louisiana-Pacific Canada Ltd. of $0.1 million at December 31, 2008 (2007 – $0.1 million). These amounts have been proportionately consolidated in Canfor's financial statements.

## 27. JOINT VENTURES

### CANFOR-LOUISIANA PACIFIC OSB LIMITED PARTNERSHIP

Canfor and Louisiana-Pacific Canada Ltd. jointly own Peace Valley OSB ("Canfor-LP OSB"), a limited partnership. Canfor has agreed to supply 330,000 cubic metres of timber annually to the joint venture from its existing timber tenure in the area where the mill is located. During 2008, Canfor made capital contributions of $3.5 million to Canfor-LP OSB (2007 – $5.5 million).

### COASTAL FIBRE LIMITED PARTNERSHIP

In March 2006, Canfor completed the transfer of its Englewood logging operation and associated timber licenses ("Englewood operations") to a new limited partnership, Coastal Fibre Limited Partnership ("CFLP"), jointly owned with Oji Paper Canada Ltd., which contributed cash of equal value. In consideration of the transfer Canfor received a partnership interest valued at $45.0 million, which approximated the book value of the assets transferred. On the same day, CFLP transferred the Englewood operations and cash of $35.0 million to Western Forest Products Inc. ("WFP") in return for a long-term agreement with WFP to supply CFLP with fibre, and CFLP will supply this fibre to HSLP.

The following balances, which represent Canfor's 50% ownership interests in Canfor-LP OSB and CFLP, have been proportionately consolidated in Canfor's consolidated financial statements:

| | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|
| (millions of dollars) | Canfor-LP OSB | CFLP | Total | Canfor-LP OSB | CFLP | Total |
| Balance Sheet | | | | | | |
| Cash | $ 2.8 | $ 0.1 | $ 2.9 | $ 3.2 | $ – | $ 3.2 |
| Other current assets | 3.0 | 0.1 | 3.1 | 2.4 | 8.3 | 10.7 |
| Property, plant and equipment | 106.5 | – | 106.5 | 115.4 | – | 115.4 |
| Deferred costs | – | – | – | 1.6 | – | 1.6 |
| Long-term fibre agreement (Notes 6, 20) | – | – | – | – | 37.1 | 37.1 |
| Accounts payable and accrued liabilities | (3.6) | (0.2) | (3.8) | (4.0) | (0.3) | (4.3) |
| Net assets | $ 108.7 | $ – | $ 108.7 | $ 118.6 | $ 45.1 | $ 163.7 |
| Statement of Loss | | | | | | |
| Sales | $ 54.8 | $ 1.7 | $ 56.5 | $ 56.0 | $ 1.4 | $ 57.4 |
| Costs and expenses | (69.1) | (1.7) | (70.8) | (78.6) | (1.4) | (80.0) |
| Net loss | $ (14.3) | $ – | $ (14.3) | $ (22.6) | $ – | $ (22.6) |
| Cash Flow Statement | | | | | | |
| Cash (used in) from operating activities | $ (3.5) | $ 0.1 | $ (3.4) | $ (6.4) | $ (0.2) | $ (6.6) |
| Cash from investing activities | 3.1 | – | 3.1 | 2.8 | – | 2.8 |
| (Decrease) increase in net cash | $ (0.4) | $ 0.1 | $ (0.3) | $ (3.6) | $ (0.2) | $ (3.8) |

## 28. SEGMENTED INFORMATION[a]

| (millions of dollars) | Lumber[d] | Panels | Pulp & Paper | Corporate & Other | Elimination Adjustment | Consolidated |
|---|---|---|---|---|---|---|
| **Year ended December 31, 2008** | | | | | | |
| **Sales to external customers[b]** | **$ 1,490.5** | **170.3** | **950.8** | **–** | **–** | **$ 2,611.6** |
| **Sales to other segments[c]** | **$ 96.0** | **3.6** | **–** | **–** | **(99.6)** | **$ –** |
| **Operating (loss) income** | **$ (155.0)** | **(56.9)** | **76.8** | **(23.0)** | **–** | **$ (158.1)** |
| **Amortization** | **$ 99.5** | **16.1** | **48.8** | **6.8** | **–** | **$ 171.2** |
| **Capital expenditures** | **$ 39.5** | **0.8** | **39.9** | **–** | **–** | **$ 80.2** |
| **Identifiable assets[e]** | **$ 1,434.4** | **248.2** | **906.6** | **611.2** | **–** | **$ 3,200.4** |
| Year ended December 31, 2007 | | | | | | |
| Sales to external customers[b] | $ 1,942.7 | 297.7 | 1,035.2 | – | – | $ 3,275.6 |
| Sales to other segments[c] | $ 111.2 | 5.0 | – | – | (116.2) | $ – |
| Operating (loss) income | $ (301.2) | (76.5) | 137.2 | (32.5) | – | $ (273.0) |
| Amortization | $ 102.8 | 23.0 | 53.3 | 5.0 | – | $ 184.1 |
| Capital expenditures | $ 47.6 | 15.7 | 24.2 | 3.1 | – | $ 90.6 |
| Identifiable assets[e] | $ 1,537.4 | 335.1 | 937.1 | 698.2 | – | $ 3,507.8 |

(a) Operations are presented by product lines.
(b) No single customer accounted for 10% or more of Canfor's total sales in 2008 and 2007.
(c) Sales to other segments are accounted for at prices that approximate market value.
(d) Sales include sales of Canfor-produced lumber of $1,214.3 million in 2008 (2007 – $1,631.8 million).
(e) Identifiable assets are presented net of an impairment charge of $169.6 million (2007 – $268.0 million), of which $2.2 million relates to the Lumber segment (2007 – $90.0 million), $81.2 million to the Panels segment (2007 – $141.4 million) and $86.2 million to Corporate and Other (2007 – $36.6 million).

### GEOGRAPHIC INFORMATION

| (millions of dollars) | **2008** | 2007 |
|---|---|---|
| **Sales by location of customer** | | |
| Canada | **$ 505.3** | $ 615.6 |
| United States | **1,378.3** | 1,855.0 |
| Europe | **174.5** | 190.3 |
| Far East and Other | **553.5** | 614.7 |
| | **$ 2,611.6** | $ 3,275.6 |
| **Capital assets and goodwill by location** | | |
| Canada | **$ 1,697.9** | $ 1,868.9 |
| United States | **186.1** | 159.5 |
| Far East and Other | **0.2** | 0.2 |
| | **$ 1,884.2** | $ 2,028.6 |

## 29. CAPITAL DISCLOSURES

Canfor'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 throughout the commodity price cycle.

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

| (millions of dollars) | **2008** | 2007 |
|---|---|---|
| Total debt (including operating loans) | **$ 622.2** | $ 496.8 |
| Less: Cash and cash equivalents | **(362.4)** | (295.5) |
| Net debt | **259.8** | 201.3 |
| Total shareholders' equity | **1,494.8** | 1,817.1 |
| | **$ 1,754.6** | $ 2,018.4 |

The Company has certain financial covenants in its debt obligations that stipulate maximum net debt to total capitalization ratios and minimum net worth amounts based on total shareholders' equity. The net debt to total capitalization is calculated by dividing total debt, less cash and cash equivalents, by shareholders' equity plus total debt less cash and cash equivalents. Debt obligations are held by various entities within the Canfor group and the individual debt agreements specify the entities within the group that are to be included in the covenant calculations.

Separately, CPLP has leverage and interest coverage ratios calculated by reference to operating earnings before interest, taxes, depreciation and amortization.

Canfor's strategy is to ensure it remains in compliance with all of its existing covenants, so as to ensure continuous access to capital, and management reviews results and forecasts to monitor Canfor's compliance. Canfor was in compliance with all its debt covenants for the years ended December 31, 2008 and 2007.

## 30. COMMITMENTS AND CONTINGENCIES

### OPERATING LEASE COMMITMENTS

Canfor has committed to operating leases for property, plant and equipment. As at December 31, 2008, the future minimum lease payments under these operating leases were as follows:

| (millions of dollars) | |
|---|---|
| 2009 | $ 22.4 |
| 2010 | 13.8 |
| 2011 | 6.6 |
| 2012 | 4.7 |
| 2013 | 2.7 |
| Thereafter | 1.8 |
| Total minimum lease payments | $ 52.0 |

### LETTERS OF CREDIT

Canfor and CPLP have several letters of credit which are summarized in Note 9, Operating Loans.

## 31. SUBSEQUENT EVENTS

### NEW OPERATING LOANS

On January 30, 2009, Canfor entered into two new operating loan facilities in the amounts of US$16.7 million ("Facility A") and US$43.7 million ("Facility B"). Facility A expires in January 2012, with the option of four one-year extensions, and is non-recourse to Canfor under normal circumstances, except for US$6.7 million. Facility B expires in January 2011, with the option of five one-year extensions, and is non-recourse to Canfor under normal circumstances. Both facilities can be drawn in Canadian or US dollars and interest is payable at floating rates based on lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus or minus a margin. The ABCP assets of Canfor have been pledged as security to support these credit facilities.

### SALE OF PANEL AND FIBRE MILL PROPERTY

On February 13, 2009, Canfor completed the sale of a property located at New Westminster, British Columbia, for gross proceeds of $47.5 million. The property was the site of Canfor's former Panel and Fibre operation, which was permanently closed at the beginning of 2008. The transaction will result in a pre-tax gain of approximately $44 million.

## 32. COMPARATIVE FIGURES

Certain 2007 figures have been reclassified to conform to the current year's presentation.

(unaudited)

## PRODUCTION

| 2008 | 1st Qtr | 2nd Qtr | 3rd Qtr | 4th Qtr | Year |
|---|---|---|---|---|---|
| Lumber SPF – MMfbm | 883.7 | 877.0 | 747.1 | 791.6 | 3,299.4 |
| Lumber SYP – MMfbm | 106.0 | 104.4 | 99.6 | 78.6 | 388.6 |
| Plywood – MMsf 3/8" basis | 89.8 | 85.7 | 44.1 | 13.8 | 233.4 |
| Oriented strand board – MMsf 3/8" basis | 158.4 | 134.3 | 85.3 | 56.8 | 434.8 |
| Pulp – 000 mt | 284.5 | 276.2 | 307.8 | 256.1 | 1,124.6 |
| Kraft paper – 000 mt | 32.4 | 34.2 | 35.9 | 30.1 | 132.6 |

| 2007 | 1st Qtr | 2nd Qtr | 3rd Qtr | 4th Qtr | Year |
|---|---|---|---|---|---|
| Lumber SPF – MMfbm | 1,114.4 | 1,080.1 | 1,050.3 | 866.8 | 4,111.6 |
| Lumber SYP – MMfbm | 99.1 | 100.7 | 96.1 | 93.3 | 389.2 |
| Plywood – MMsf 3/8" basis | 100.9 | 101.2 | 89.8 | 93.1 | 385.0 |
| Oriented strand board – MMsf 3/8" basis | 179.9 | 166.9 | 158.8 | 167.6 | 673.2 |
| Pulp – 000 mt | 305.4 | 308.8 | 317.1 | 313.2 | 1,244.5 |
| Kraft paper – 000 mt | 31.6 | 33.9 | 33.0 | 33.1 | 131.6 |

## SHIPMENTS

| 2008 | 1st Qtr | 2nd Qtr | 3rd Qtr | 4th Qtr | Year |
|---|---|---|---|---|---|
| Lumber – MMfbm | | | | | |
| Canfor produced SPF | 862.7 | 935.3 | 755.9 | 834.3 | 3,388.2 |
| Canfor produced SYP | 110.3 | 125.9 | 110.3 | 86.2 | 432.7 |
| Purchased from other wholesale producers | 49.5 | 46.0 | 39.8 | 35.7 | 171.0 |
| Total Lumber | 1,022.5 | 1,107.2 | 906.0 | 956.2 | 3,991.9 |
| Plywood – MMsf 3/8" basis | 86.0 | 95.7 | 54.2 | 28.2 | 264.1 |
| Oriented strand board – MMsf 3/8" basis | 163.8 | 152.9 | 90.5 | 55.7 | 462.9 |
| Pulp – 000 mt | | | | | |
| Canfor produced | 279.0 | 289.4 | 284.0 | 235.6 | 1,088.0 |
| Marketed on behalf of HSLP | 78.3 | 96.2 | 86.0 | 52.6 | 313.1 |
| Total Pulp | 357.3 | 385.6 | 370.0 | 288.2 | 1,401.1 |
| Kraft paper – 000 mt | 35.1 | 33.7 | 31.7 | 24.3 | 124.8 |

| 2007 | 1st Qtr | 2nd Qtr | 3rd Qtr | 4th Qtr | Year |
|---|---|---|---|---|---|
| Lumber – MMfbm | | | | | |
| Canfor produced SPF | 1,002.0 | 1,122.0 | 1,121.1 | 988.4 | 4,233.5 |
| Canfor produced SYP | 108.1 | 126.1 | 111.2 | 103.3 | 448.7 |
| Purchased from other wholesale producers | 102.6 | 96.4 | 69.0 | 57.2 | 325.2 |
| Total Lumber | 1,212.7 | 1,344.5 | 1,301.3 | 1,148.9 | 5,007.4 |
| Plywood – MMsf 3/8" basis | 86.9 | 118.7 | 89.5 | 90.3 | 385.4 |
| Oriented strand board – MMsf 3/8" basis | 173.8 | 168.0 | 161.8 | 166.3 | 669.9 |
| Pulp – 000 mt | | | | | |
| Canfor produced | 304.3 | 309.3 | 307.0 | 308.3 | 1,228.9 |
| Marketed on behalf of HSLP | 81.4 | 102.5 | 89.4 | 93.3 | 366.6 |
| Total Pulp | 385.7 | 411.8 | 396.4 | 401.6 | 1,595.5 |
| Kraft paper – 000 mt | 30.4 | 35.9 | 30.8 | 32.4 | 129.5 |

## 2008 SELECTED QUARTERLY FINANCIAL INFORMATION

| (unaudited) | 1st Qtr | 2nd Qtr | 3rd Qtr | 4th Qtr | Year |
|---|---|---|---|---|---|
| **Sales and income** (millions of dollars) | | | | | |
| Sales | $ 648.5 | $ 706.4 | $ 668.0 | $ 588.7 | $ 2,611.6 |
| Manufacturing and product costs | 574.4 | 447.0 | 459.2 | 472.5 | 1,953.1 |
| Freight and other distribution costs | 115.1 | 129.7 | 114.3 | 117.1 | 476.2 |
| Export tax, countervailing and anti-dumping duties | 13.4 | 18.2 | 17.5 | 6.0 | 55.1 |
| Amortization | 43.5 | 41.5 | 42.2 | 44.0 | 171.2 |
| Selling and administration costs | 15.8 | 15.2 | 16.6 | 13.0 | 60.6 |
| Restructuring, mill closure and severance costs | 3.8 | 34.0 | 5.4 | 10.3 | 53.5 |
| **Operating loss** | (117.5) | 20.8 | 12.8 | (74.2) | (158.1) |
| Interest income (expense), net | (5.3) | (5.7) | (6.7) | (7.7) | (25.4) |
| Foreign exchange gain (loss) on long-term debt and investments | (12.0) | (0.1) | (16.2) | (72.0) | (100.3) |
| Gain (loss) on derivative financial instruments | 6.0 | 26.0 | (38.8) | (81.7) | (88.5) |
| North Central Plywood mill fire, net | – | 57.9 | – | – | 57.9 |
| Prince George Pulp & Paper mill fire, net | 8.5 | – | – | (0.3) | 8.2 |
| Asset impairments | – | – | (70.0) | (99.6) | (169.6) |
| Other income (expense) | 1.2 | (1.5) | 0.1 | 12.9 | 12.7 |
| Net loss before income taxes and non-controlling interests | (119.1) | 97.4 | (118.8) | (322.6) | (463.1) |
| Income tax recovery (expense) | 55.7 | (24.0) | 30.0 | 80.2 | 141.9 |
| Non-controlling interests | (22.0) | (9.2) | (5.4) | 12.6 | (24.0) |
| **Net loss** | $ (85.4) | $ 64.2 | $ (94.2) | $ (229.8) | $ (345.2) |
| **Per common share** (dollars) | | | | | |
| Net loss | | | | | |
| Basic and diluted | $ (0.60) | $ 0.45 | $ (0.66) | $ (1.61) | $ (2.42) |
| **Cash generated from (used in)** (millions of dollars) | | | | | |
| Operating activities | $ (6.7) | $ 80.2 | $ 63.3 | $ 20.9 | $ 157.7 |
| Financing activities | | | | | |
| Long-term debt | (14.8) | – | – | – | (14.8) |
| Other | (9.8) | (11.9) | (14.0) | 8.1 | (27.6) |
| | (24.6) | (11.9) | (14.0) | 8.1 | (42.4) |
| Investing activities | | | | | |
| Additions to property, plant, equipment and timber | (19.3) | (16.8) | (22.2) | (21.9) | (80.2) |
| Other | (3.4) | 4.6 | 9.5 | 21.1 | 31.8 |
| | (22.7) | (12.2) | (12.7) | (0.8) | (48.4) |
| **Increase (decrease) in cash and cash equivalents** | $ (54.0) | $ 56.1 | $ 36.6 | $ 28.2 | $ 66.9 |

Certain previously published figures have been reclassified to conform to the current presentation.

| (unaudited) | 1st Qtr | 2nd Qtr | 3rd Qtr | 4th Qtr | Year |
|---|---|---|---|---|---|
| **Sales and income** (millions of dollars) | | | | | |
| **Sales** | $ 850.6 | $ 876.6 | $ 837.4 | $ 711.0 | $ 3,275.6 |
| Manufacturing and product costs | 662.1 | 662.0 | 649.0 | 610.5 | 2,583.6 |
| Freight and other distribution costs | 143.3 | 152.7 | 141.5 | 127.5 | 565.0 |
| Export tax, countervailing and anti-dumping duties | 28.7 | 29.2 | 26.5 | 17.4 | 101.8 |
| Amortization | 47.8 | 43.5 | 45.6 | 47.2 | 184.1 |
| Selling and administration costs | 26.5 | 18.9 | 15.8 | 11.6 | 72.8 |
| Restructuring, mill closure and severance costs | – | 8.7 | 11.1 | 21.5 | 41.3 |
| **Operating loss** | (57.8) | (38.4) | (52.1) | (124.7) | (273.0) |
| Interest income (expense), net | 0.6 | (3.3) | (2.4) | (4.3) | (9.4) |
| Foreign exchange gain (loss) on long-term debt and investments | (6.0) | 16.8 | 9.5 | (4.1) | 16.2 |
| Gain (loss) on derivative financial instruments | 8.6 | (7.7) | 8.9 | 6.2 | 16.0 |
| Asset impairments | (5.0) | – | (7.0) | (256.0) | (268.0) |
| Other income (expense) | 15.2 | (13.7) | (9.3) | (3.3) | (11.1) |
| Net loss before income taxes and non-controlling interests | (44.4) | (46.3) | (52.4) | (386.2) | (529.3) |
| Income tax recovery | 26.0 | 25.6 | 27.2 | 155.3 | 234.1 |
| Non-controlling interests | (24.3) | (18.1) | (16.9) | (6.1) | (65.4) |
| **Net loss** | $ (42.7) | $ (38.8) | $ (42.1) | $ (237.0) | $ (360.6) |
| **Per common share** (dollars) | | | | | |
| Net loss | | | | | |
| Basic and diluted | $ (0.30) | $ (0.27) | $ (0.30) | $ (1.66) | $ (2.53) |
| **Cash generated from (used in)** (millions of dollars) | | | | | |
| Operating activities | $ (556.7) | $ 21.8 | $ 102.7 | $ (50.9) | $ (483.1) |
| Financing activities | | | | | |
| Long-term debt | (41.6) | (11.7) | (37.5) | (8.3) | (99.1) |
| Other | (20.0) | (19.0) | (18.7) | (17.5) | (75.2) |
| | (61.6) | (30.7) | (56.2) | (25.8) | (174.3) |
| Investing activities | | | | | |
| Additions to property, plant, equipment and timber | (18.3) | (21.1) | (23.7) | (27.5) | (90.6) |
| Other | 50.8 | 56.0 | (83.0) | (4.1) | 19.7 |
| | 32.5 | 34.9 | (106.7) | (31.6) | (70.9) |
| **Increase (decrease) in cash and cash equivalents** | $ (585.8) | $ 26.0 | $ (60.2) | $ (108.3) | $ (728.3) |

Certain previously published figures have been reclassified to conform to the current presentation.

## FIVE-YEAR COMPARATIVE REVIEW

| (unaudited) | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|
| **Sales and income** (millions of dollars) | | | | | |
| **Sales** | $ 2,611.6 | $ 3,275.6 | $ 3,842.3 | $ 3,787.1 | $ 3,925.0 |
| Manufacturing and product costs | 1,953.1 | 2,583.6 | 2,949.8 | 2,597.7 | 2,382.8 |
| Freight and other distribution costs | 476.2 | 565.0 | 598.3 | 593.3 | 525.8 |
| Export tax, countervailing and anti-dumping duties | 55.1 | 101.8 | 109.8 | 224.8 | 276.2 |
| Amortization | 171.2 | 184.1 | 182.6 | 151.6 | 140.3 |
| Selling and administration costs | 60.6 | 72.8 | 78.5 | 72.0 | 68.9 |
| Restructuring, mill closure and severance costs | 53.5 | 41.3 | 6.5 | 5.3 | 36.5 |
| Countervailing and anti-dumping duty refund | – | – | (717.7) | – | – |
| **Operating income (loss) from continuing operations** | (158.1) | (273.0) | 634.5 | 142.4 | 494.5 |
| Interest income (expense), net | (25.4) | (9.4) | 56.2 | (42.2) | (58.8) |
| Foreign exchange gain on long-term debt and investments | (100.3) | 16.2 | 4.7 | 10.0 | 48.7 |
| Gain on derivative financial instruments | (88.5) | 16.0 | – | – | – |
| Asset impairments | (169.6) | (268.0) | (19.1) | – | – |
| Other income (expense) | 12.7 | (11.1) | (10.5) | 12.8 | 8.2 |
| Unusual items | 66.1 | – | – | (8.8) | – |
| Net Income (loss) from continuing operations before income taxes and non-controlling interests | (463.1) | (529.3) | 665.8 | 114.2 | 492.6 |
| Income tax recovery (expense) | 141.9 | 234.1 | (169.4) | (12.4) | (94.1) |
| Non-controlling interests | (24.0) | (65.4) | (20.7) | – | – |
| **Net Income (loss) from continuing operations** | (345.2) | (360.6) | 475.7 | 101.8 | 398.5 |
| Net income (loss) from discontinued operations | – | – | (3.9) | (5.8) | 17.0 |
| **Net income (loss)** | $ (345.2) | $ (360.6) | $ 471.8 | $ 96.0 | $ 415.5 |
| **Per common share** (in dollars) | | | | | |
| Net Income (loss) from continuing operations | | | | | |
| Basic | $ (2.42) | $ (2.53) | $ 3.34 | $ 0.71 | $ 3.31 |
| Diluted | (2.42) | (2.53) | 3.34 | 0.71 | 3.09 |
| Net income (loss) | | | | | |
| Basic | (2.42) | (2.53) | 3.31 | 0.67 | 3.45 |
| Diluted | (2.42) | (2.53) | 3.31 | 0.67 | 3.22 |
| Book value per share | 10.48 | 12.74 | 15.63 | 14.36 | 13.72 |
| **Assets and capitalization** (millions of dollars) | | | | | |
| Working capital | $ 531.4 | $ 815.2 | $ 1,172.3 | $ 725.7 | $ 809.7 |
| Long-term investments and other | 125.7 | 170.4 | 115.3 | 186.5 | 196.8 |
| Property, plant, equipment and timber | 1,798.5 | 1,959.4 | 2,254.9 | 2,211.1 | 2,141.7 |
| Goodwill | 85.7 | 69.2 | 81.6 | – | – |
| Deferred charges | 110.2 | 90.0 | 91.8 | 96.9 | 96.1 |
| Net assets of discontinued operations | – | – | – | 73.8 | 127.6 |
| Net assets | $ 2,651.5 | $ 3,104.2 | $ 3,715.9 | $ 3,294.0 | $ 3,371.9 |
| Long-term debt | $ 428.7 | $ 481.6 | $ 602.8 | $ 544.5 | $ 660.5 |
| Long-term accrued liabilities and obligations | 208.8 | 203.5 | 173.3 | 220.5 | 218.2 |
| Future income taxes | 242.4 | 299.5 | 415.4 | 468.3 | 499.2 |
| Deferred credit | – | – | – | 14.1 | 27.2 |
| Non-controlling interests | 276.8 | 302.5 | 296.7 | – | – |
| Shareholders' equity | 1,494.8 | 1,817.1 | 2,227.7 | 2,046.6 | 1,966.8 |
| Total capitalization | $ 2,651.5 | $ 3,104.2 | $ 3,715.9 | $ 3,294.0 | $ 3,371.9 |
| **Additions to property, plant, equipment and timber** (millions of dollars) | $ 80.2 | $ 90.6 | $ 107.1 | $ 334.5 | $ 202.5 |

Certain prior years' figures have been reclassified to conform to the 2008 presentation.

| (unaudited) | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|
| **Cash generated from (used in)** (millions of dollars) | | | | | |
| Operating activities | $ 157.7 | $ (483.1) | $ 1,140.2 | $ 193.3 | $ 708.5 |
| Financing activities | | | | | |
| Long-term debt | (14.8) | (99.1) | 26.5 | (67.8) | 42.0 |
| Common shares | – | 0.4 | 0.3 | (11.9) | 8.0 |
| Cash distributions paid to non-controlling interests | (52.3) | (74.2) | (17.6) | – | – |
| Other | (24.7) | (1.4) | (23.5) | (1.6) | (0.8) |
| | (42.4) | (174.3) | (14.3) | (81.3) | 49.2 |
| Investing activities | | | | | |
| Property, plant, equipment and timber, net | (74.6) | (86.6) | (104.3) | (327.0) | (192.6) |
| Temporary investments | – | 124.5 | (119.0) | 3.0 | – |
| Howe Sound Pulp and Paper Limited Partnership | (11.5) | – | – | (50.0) | – |
| Business acquisitions | (0.8) | (16.8) | (206.1) | – | – |
| Investment in subsidiaries and affiliates | – | – | – | – | (38.2) |
| Changes in long-term investments | – | (85.9) | – | – | – |
| Other | 38.5 | (6.1) | 11.8 | 125.2 | 14.0 |
| | (48.4) | (70.9) | (417.6) | (248.8) | (216.8) |
| Increase (decrease) in cash and cash equivalents | | | | | |
| From continuing operations | 66.9 | (728.3) | 708.3 | (136.8) | 540.9 |
| From discontinued operations | – | – | 16.6 | 7.4 | (19.3) |
| | $ 66.9 | $ (728.3) | $ 724.9 | $ (129.4) | $ 521.6 |
| **Financial statistics** | | | | | |
| EBITDA | 13.1 | (88.9) | 817.1 | 294.0 | 634.8 |
| Return on capital employed | (16.4)% | (15.6)% | 16.0% | 4.9% | 19.8% |
| Return on common shareholders' equity | (18.5)% | (17.8)% | 22.1% | 4.8% | 28.6% |
| Ratio of current assets to current liabilities | 2.0:1 | 3.0:1 | 2.2:1 | 2.4:1 | 2.4:1 |
| Ratio of net debt to capitalization | 15% | 10% | (26)% | 14% | 13% |
| **Production statistics*** | | | | | |
| Lumber SPF – MMfbm | 3,299.4 | 4,111.6 | 4,459.8 | 4,624.4 | 4,234.9 |
| Lumber SYP– MMfbm | 388.6 | 389.2 | 341.4 | – | – |
| Plywood – MMsf 3/8" basis | 233.4 | 385.0 | 439.2 | 433.3 | 356.6 |
| Oriented strand board – MMsf 3/8" basis | 434.8 | 673.2 | 734.4 | 478.8 | 384.8 |
| Pulp – 000 mt | 1,124.6 | 1,244.5 | 1,209.8 | 1,189.1 | 1,142.3 |
| Kraft paper – 000 mt | 132.6 | 131.6 | 129.1 | 127.4 | 134.1 |
| Hardboard – MMsf 3/8" basis | – | 26.2 | 27.3 | 29.4 | 29.4 |
| Refined fibre – 000 mt | – | 25.5 | 34.8 | 35.9 | 37.4 |
| **Sales by product line*** | | | | | |
| Lumber – Canfor produced | 47% | 49% | 50% | 59% | 60% |
| Pulp and kraft paper | 36 | 32 | 25 | 25 | 25 |
| Plywood | 3 | 4 | 4 | 4 | 4 |
| Lumber – other producers | 2 | 4 | 11 | 6 | 5 |
| Oriented Strand Board | 3 | 4 | 4 | 4 | 4 |
| Miscellaneous | 9 | 7 | 6 | 2 | 2 |
| | 100% | 100% | 100% | 100% | 100% |
| **Sales by market** | | | | | |
| United States | 53% | 57% | 67% | 67% | 61% |
| Canada | 19 | 19 | 15 | 12 | 20 |
| Far East | 20 | 17 | 13 | 13 | 12 |
| Europe | 7 | 6 | 4 | 7 | 7 |
| Other | 1 | 1 | 1 | 1 | 0 |
| | 100% | 100% | 100% | 100% | 100% |

* Excludes discontinued operations

Certain prior years' figures have been reclassified to conform to the 2008 presentation.

# DIRECTORS AND OFFICERS

## DIRECTORS

The names, principal occupations, municipalities of residence and dates of appointment of the Directors of the Company, are as below. For more information visit www.canfor.com.

**P.J.G. Bentley**, O.C., LL.D. [1][2][3][4][5][6]
Chairman of the Board
Canfor Corporation
Vancouver, British Columbia
Director since 1966

**R.L. Cliff**, C.M., F.C.A. [1][2]
Chairman of the Board,
Heathcliff Properties Ltd.
West Vancouver, British Columbia
Director since 1983

**M.J. Korenberg** [1][3][6]
Managing Director, Vice-Chairman
The Jim Pattison Group
West Vancouver, British Columbia
Director since 2003

**J.A. Pattison**, O.C., O.B.C. [2][4]
President, Managing Director,
Chief Executive Officer and Chairman
The Jim Pattison Group
West Vancouver, British Columbia
Director since 2003

**Conrad A. Pinette** [4][6]
President
Condor Holdings
Vancouver, British Columbia
Director since 2008

**D.C. Selman**, F.C.A. [1][3][5][6]
Senior Consultant, Wolrige Mahon
Richmond, British Columbia
Director since 2004

**J.F. Shepard**, P.Eng. [4][6]
President and Chief Executive Officer
Canfor Corporation
Vancouver, British Columbia
Director since 2007

**J. McNeil Singleton** [4][6]
President and Chief Executive Officer
New South Companies, Inc.
Myrtle Beach, South Carolina
Director since 2007

**T.A. Tutsch** [2][3][5]
Corporate Director
E. Nester & Associates
Toronto, Ontario
Director since 2007

## OFFICERS

The names and municipalities of residence of the officers of the Company and the offices held by each of them are as below. For more information visit www.canfor.com.

**P.J.G.Bentley**
Chairman
Vancouver, British Columbia

**J.F. Shepard**
President and Chief Executive Officer
Vancouver, British Columbia

**T. Sitar**
Vice-President Finance and Chief Financial Officer
Vancouver, British Columbia

**D.M. Calabrigo**
Vice-President, Corporate Development,
General Counsel and Corporate Secretary
Surrey, British Columbia

**M.A. Feldinger**
Vice President, Wood Products Manufacturing
Prince George, British Columbia

**K.O. Higginbotham**
Vice-President, Forestry and Environment
Surrey, British Columbia

**D.B. Kayne**
Vice-President, Wood Products Marketing and Sales
Tsawwassen, British Columbia

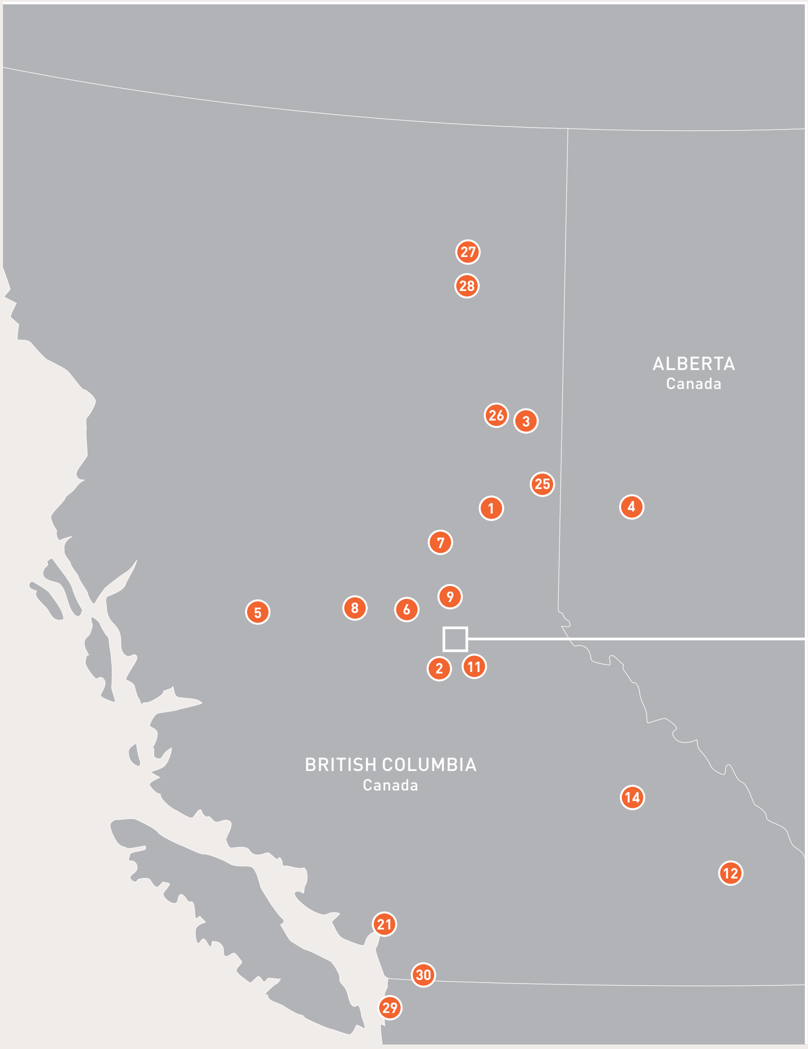
**R. Stewart**
Vice-President, Human Resources
Delta, British Columbia

**A.L.W. Cook**
Vice-President, Capital Projects
Surrey, British Columbia

(1) Member of the Audit Committee, which reviews the Company's financial statements, the scope and results of the external auditor's work, the adequacy of internal accounting and audit programs and compliance with accounting and reporting standards.
(2) Member of the Management Resources and Compensation Committee, which oversees human resources and compensation policies and ensures management development and succession programs are in place.
(3) Member of the Corporate Governance Committee, which ensures that the Company through its Board of Directors sustains an effective approach to corporate governance.
(4) Member of the Environmental, Health and Safety Committee, which develops, reviews and makes recommendations on matters related to the Company's environmental, health and safety policies, and monitors compliance with those policies and with government regulations.
(5) Member of the Pension Committee, which oversees the administration, financial reporting and investment activities of the Company's pension plans.
(6) Member of the Capital Expenditure Committee, which reviews proposed capital expenditures.

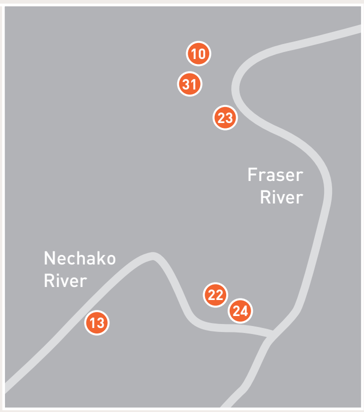
The term of office of each Director expires on the date of the next Annual General Meeting of the Company.

WESTERN CANADA




EAST COAST


PRINCE GEORGE




## SAWMILLS

Chetwynd . . . . . . . . . . . . . . 1
Clear Lake . . . . . . . . . . . . . 2
Fort St John . . . . . . . . . . . . 3
Grande Prairie . . . . . . . . . . 4
Houston. . . . . . . . . . . . . . . . 5
Isle Pierre. . . . . . . . . . . . . . 6
Mackenzie. . . . . . . . . . . . . . 7
Plateau . . . . . . . . . . . . . . . . 8
Polar . . . . . . . . . . . . . . . . . . 9
Prince George . . . . . . . . . 10
Quesnel. . . . . . . . . . . . . . . 11
Radium . . . . . . . . . . . . . . . 12
Rustad. . . . . . . . . . . . . . . . 13
Vavenby. . . . . . . . . . . . . . . 14
Daaquam. . . . . . . . . . . . . . 15
Graham, NC . . . . . . . . . . . 16
Camden, SC . . . . . . . . . . . 17
Conway, SC. . . . . . . . . . . . 18
Marion, SC . . . . . . . . . . . . 19
Darlington, SC . . . . . . . . . 20

## PULP & PAPER

Howe Sound [2]. . . . . . . . . . 21
Intercontinental [1]. . . . . . . 22
Northwood [1]. . . . . . . . . . . 23
Prince George [1] . . . . . . . . 24
Taylor. . . . . . . . . . . . . . . . . 25

## PLYWOOD & OSB

Peace Valley OSB [2] . . . . . . 26
PolarBoard OSB . . . . . . . 27
Tackama Plywood . . . . . . 28

## OTHER

Bellingham, WA. . . . . . . . 29
Uneeda . . . . . . . . . . . . . . . 30
J.D. Little Forest Centre. . 31

(1) Canfor Pulp Limited Partnership – 50.2% ownership
(2) Limited Partnership – 50% ownership

## MILL OPERATIONS

| | 2008 Production | Capacity |
|---|---|---|
| **LUMBER** (MMfbm) | | |
| Chetwynd | 40.4 | |
| Clear Lake | 102.8 | |
| Daaquam | 119.0 | |
| Fort St John | 180.5 | |
| Grande Prairie | 216.2 | |
| Houston | 437.3 | |
| Isle Pierre | 267.0 | |
| Mackenzie | 75.3 | |
| Plateau | 445.2 | |
| Polar | 210.6 | |
| Prince George | 306.3 | |
| Quesnel | 335.7 | |
| Radium | 164.0 | |
| Rustad | 245.7 | |
| Vavenby | 153.4 | |
| **Total SPF** | 3,299.4 | 4,356 |
| Graham | 136.3 | |
| Camden | 123.0 | |
| Conway | 75.0 | |
| Darlington | 54.3 | |
| **Total SYP** | 388.6 | 552 |
| **Total Lumber** | 3,688.0 | 4,908 |
| **PLYWOOD** (MMsf 3/8" basis) | | |
| North Central Plywoods [1] | 76.3 | |
| Tackama | 157.1 | |
| **Total Plywood** | 233.4 | 270 |
| **OSB** (MMsf 3/8" basis) | | |
| Peace Valley [2] | 608.9 | |
| Polarboard | 130.3 | |
| **Total OSB** | 739.2 | 1,460 |
| **PULP** (000 tonnes) | | |
| Howe Sound Pulp and Paper LP [2] | 325.5 | |
| Intercon [2] | 271.6 | |
| Northwood [2] | 544.1 | |
| PG Pulp [2] | 117.1 | |
| Taylor Pulp | 191.8 | |
| **Total Pulp** | 1,450.1 | 1,673 |
| **PAPER** (000 tonnes) | | |
| PG Paper [2] | 132.6 | 140 |
| **NEWSPRINT** (000 tonnes) | | |
| Howe Sound Pulp and Paper LLP [2] | 211.4 | 230 |

(1) Closed due to fire, May 2008.
(2) Partly owned – includes 100% of production.

## DEFINITIONS OF SELECTED FINANCIAL TERMS

**Book Value per Share** is the shareholders' equity, at the end of the year, divided by the number of common shares outstanding at the end of the year.

**Capital Employed** consists of the funds invested or retained in Canfor in the form of shares or liabilities. It is composed of unpresented cheques, current bank loans (net of cash and temporary investments), current portion of long-term debt, long-term debt, future income taxes arising from timing differences and shareholders' equity. Long-term liabilities and other accruals such as deferred reforestation costs, unfunded pension and post employment benefits, and unrealized foreign exchange losses on long-term debt are specifically excluded because they do not represent borrowed funds or funds invested by shareholders.

**Earnings Before Interest, Taxes and Amortization (EBITDA)** represents operating income before amortization.

**Net Debt** is total debt less cash and temporary investments.

**Net Income (Loss) per Common Share** is calculated as described in Note 23 to the Consolidated Financial Statements.

**Return on Capital Employed** is equal to net income plus interest, after tax, divided by the average of the capital employed during of the year.

**Return on Common Shareholders' Equity** is equal to net income for the year, divided by the average of total shareholders' equity at the beginning and end of the year.

## CORPORATE AND SHAREHOLDER INFORMATION

**Annual General Meeting**
Canfor's Annual General Meeting will be held at the Fairmont Hotel Vancouver, Saturna Island Room, 900 West Georgia Street, Vancouver, B.C., on Thursday April 30th, 2009 at 11:30 a.m.

**Auditors**
PricewaterhouseCoopers
Vancouver, BC

**Transfer Agent and Registrar**
CIBC Mellon Trust Company
Vancouver, Calgary, Regina, Winnipeg, Toronto, Montreal and Halifax

**Stock Listing**
Toronto Stock Exchange
Symbol: CFP

**Investor Contact**
Patrick Elliott
Treasurer
Telephone: (604) 661-5441
Fax: (604) 661-5429
Email: patrick.elliott@canfor.com

**Canfor Corporation Head Office**
#100 – 1700 West 75th Avenue
Vancouver, BC V6P 6G2
Telephone: (604) 661-5241
Fax: (604) 661-5235
Email: info@canfor.com
Web: www.canfor.com

Canfor also produces an Annual Information Form. To obtain this publication or more information about the company, please contact Canfor Corporation, Public Affairs or visit our website at www.canfor.com/investors

**Public Affairs Contact**
Dave Lefebvre
Director, Public Affairs &
Corporate Communications
Telephone: (604) 661-5225
Fax: (604) 661-5219
Email: dave.lefebvre@canfor.com

This annual report has been printed on Monadnock Astrolite Silk paper which is made with a percentage of CPLP's NBSK Pulp.

www.canfor.com

CANFOR CORPORATION SUSTAINABILITY REPORT 2008

The publication of our Sustainability Report is in keeping with our commitment to be transparent about the way we conduct ourselves while carrying out our business operations. This includes reporting on our commitment to operating in an environmentally responsible manner, our initiatives to create a safe work environment for employees and our contributions to enhance the communities where we live and work.

# FORESTRY REPORT

At the heart of Canfor's forestry operations is its forest management system (FMS). The FMS is a systematic means of identifying, addressing and managing environmental impacts and sustainable forest management commitments within Canfor's Woodlands operations.

The goal of the system is to maintain and enhance the long term health of forest ecosystems, for the benefit of all living things both locally and globally, while providing the environmental, economic and social opportunities for the benefit of both present and future generations.

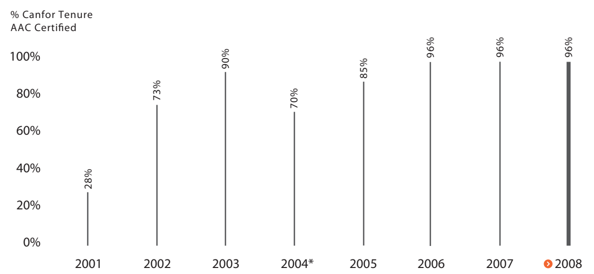
All of our practices in the forests that we mange are covered by our FMS, which is independently certified to the latest version of the International Organization for Standardization (ISO) Environmental Management System (EMS) standard CAN/CSA-ISO 14001:04.

## SUSTAINABLE FOREST MANAGEMENT CERTIFICATION

Canfor continues to be a leader in sustainable forest management certification. In addition to its EMS certification, 96% of its allowable annual cut under forest tenures is independently certified to the Canadian Standards Association (CSA) standard for Sustainable Forest Management (CAN.CSA-Z809-02). .

As of 2008, Canfor has 16 facilities certified to the Programme for the Endorsement of Forest Certification Schemes (PEFC): Chain of Custody of Forest Based Products – Requirements Standard.

SFM CERTIFICATION STATUS




*Canfor acquired Slocan and associated crown tenures

WILDLIFE AND HABITAT MANAGEMENT

In 2008, Canfor continued conservation planning for species at risk by participating with provincial governments in both BC and Alberta, key environmental groups and other stakeholders. Key initiatives designed to assist with the recovery of Woodland Caribou continue to be implemented at our Grande Prairie operations in Alberta. Canfor's Vavenby division continued to work with government agencies on planning for the recovery of Mountain Caribou poplulations in the North Thompson Valley of BC. Final comments were provided to agencies in the fall of 2008 and government published a regulation in December 2008 setting out its expectations for mountain Caribou habitat protection and management.

## COMPLIANCE WITH REGULATIONS

Canfor is committed to maintaining a transparent system for environmental reporting, including compliance reporting. During 2008, Canfor's forestry operations had a total of 4 non-compliance incidents on the company's forest tenures. In each case, the company took the necessary actions to mitigate any environmental consequences and correct conditions that may have led to the incidents.

Canfor forestry operations also had one minor spill, which was promptly reported to the appropriate government agencies. The spill was immediately contained and properly cleaned up.

## FPAC SUSTAINABILITY INITIATIVE AND REPORT – INDUSTRY COMMITS TO CARBON NEUTRALITY

As active members of the Forest Products Association of Canada's (FPAC) Sustainability Initiative, Canfor is committed to its principles of operating in a manner that is environmentally responsible, socially desirable and economically viable. As a participant in this initiative, Canfor will integrate these principles in our business practices and contribute to sustainable development through continual improvement.

The industry has set a number of targets for itself, including Carbon neutrality by 2015 (a target the Canadian forest products industry established under an ambitious new climate change plan unveiled by FPAC at the end of October 2007). The industry has pledged to accomplish its goal without resorting to offsets.

To meet the 2015 target, FPAC members will seek to minimize their carbon footprint by reducing direct and indirect emissions, increasing the carbon sequestration potential of forests and products and increasing avoided emissions. Specifically, efforts will focus on:

- Becoming energy self-sufficient—switching from fossil fuels to renewable energy sources
- Adopting new, more energy-efficient technologies
- Increasing diversion of used products from landfills
- Increasing the use of landfill capping systems (to prevent methane leaks)
- Increasing cogeneration opportunities
- Identifying opportunities to maintain and enhance carbon storage in forests through landscape planning and sustainable forest management practices
- Maximizing recycling of paper and wood products

## OBJECTIVES AND TARGETS FOR 2009

### FOREST MANAGEMENT SYSTEM

We will maintain the Forest Management System during 2008. Surveillance audits to the ISO 14001 standard will be carried out at 4 operations during 2009.

In 2008, 11 sites had their environmental management systems re-certified to the ISO-14001 standard.

### SUSTAINABLE FOREST MANAGEMENT CERTIFICATION

We will maintain existing CSA SFM certifications. In 2008, 11 sites were re-certified to the CSA Z809 –02 standard.

### SFM AUDITS

In 2009, Canfor will undertake 13 internal audits and 13 external audits, encompassing CSA, ISO, PEFC and OSHA standards.

# MANUFACTURING

## COMPLIANCE REPORT

Canfor is committed to transparency in our environmental reporting and includes compliance reporting as part of this process. The following is an inventory of compliance for Canfor's wholly-owned manufacturing operations.

In 2008, Canfor had the following non-compliance situations (reported in accordance with government non-compliance reporting criteria):

### AIR

At wood products operations, excessive emissions were observed from a planer cyclone by the ministry of environment; a baghouse aborted to the atmosphere on three occasions in one day due to mechanical issues; a burner operated below compliance temperature for a portion of one operating day due to mechanical issues and wet fuel; another burner operated below compliance temperature due to fuel conveyor issues; a third burner was out of compliance for portions of four operating days due to heavy snowfall or mechanical problems related to very cold weather. As concerns the planer cyclone, capital expenditure approval is being sought for modifications to improve the performance; in the other instances mechanical problems were corrected and/or weather related issues ceased with improvements in the weather.

### EFFLUENT

No issues in 2008.

### LANDFILL

In 2008, Canfor had compliance issues with landfills at 4 operations as follows: at one wood products operation a Ministry of Environment inspection indicated an unauthorized historical deposit of chips and subsequently issued an information order to Canfor; at another operation leachate was found discharging from a wood residue landfill; at another operation leachate was being generated from decomposition of an historical deposit of chips; at another operation landfill quantities were in excess of permitted limits and at another operation the landfill was found to be out of compliance due to wood debris greater than 1 metre in length in the landfill, excessive slopes, standing water in an ash disposal area and leachate at the base of the landfill. In all cases, management plans have been implemented or are in the process of being implemented to address the compliance issues and prevent recurrence. Steps have also been taken to ensure that other operations are managing their landfills in compliance with permit conditions.

SPILLS

Canfor manufacturing operations had 2 reportable spills in 2008. All were contained, cleaned up and preventive actions taken. The spills included: one spill of hydraulic oil due to a ruptured hose and one spill of thermal oil due to a drum punctured by a forklift.

## PERFORMANCE VERSUS OBJECTIVES IN 2008

AIR QUALITY

We will work with other industry representatives and the BC Ministry of Environment to develop an achievable phase out program for BC's remaining Tier 2 beehive burners.

PERFORMANCE

Development of a Tier 2 beehive burner phase out program is still in progress. In 2008, Canfor shut Tier 2 burners at two sawmills as a result of fibre supply agreements with third parties: a pulp mill for generation of heat and power, and a wood pellet producer..

AUDITS

We will conduct corporate environmental audits of five sawmills and one panel plant.

PERFORMANCE

Audits were conducted at five sawmills as planned. The NCP panel plant audit did not occur as the plant was destroyed by a fire.

## OBJECTIVES AND TARGETS FOR 2009

In BC, we will continue to work towards phasing out Canfor's remaining Tier 2 burners. Canfor currently has one operating Tier 2 burner.

AUDITS

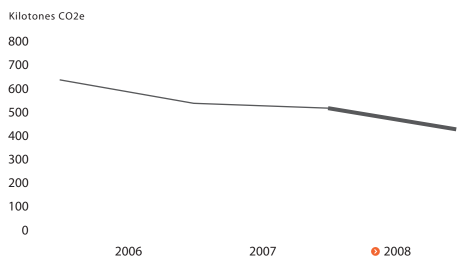
We will conduct corporate environmental audits of five sawmills and one remanufacturing plant.

## IMPROVING OUR PERFORMANCE

Canfor's GHG emissions were lower in 2008 compared with 2007 largely due to reduced operational levels, including indefinite closures of three operations and permanent closure of another that usednatural gas for veneer or lumber drying.

Wood residue usage has increased to over 90% in 2008, from 53% of total residue generated in 2004. Increased usage in 2008 over 2007 was in part due to permanent shutdown of Canfor's one remaining Tier 1 beehive burner at Fort St. John in April 2008 and wood residue being sold to third parties including the oil and gas industry, a local pulp mill and the Grande Prairie cogeneration facility. Reduced operational levels also reduced wood residue supply and increased external demand for that reduced supply.

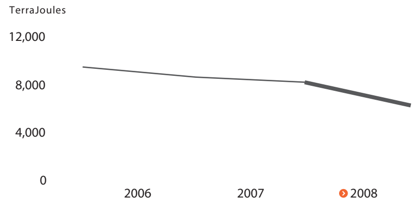
### CANFOR GREENHOUSE GAS EMISSIONS*




Canfor's GHG emissions declinded in 2008 largely due to wood product facility curtailments..

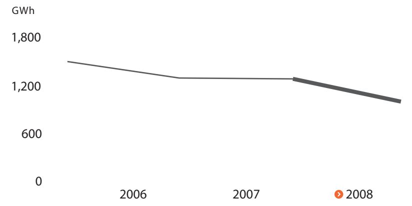
*Includes emissions by CPLP (50% ownership)

## CANFOR NATURAL GAS USE



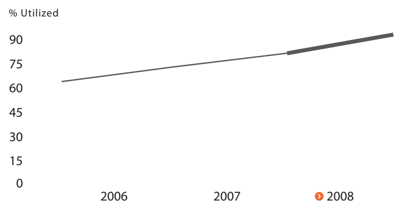

Natural Gas usage was less in 2008 due to wood product facility curtailments.

## CANFOR ELECTRICITY PURCHASES




Electricuty purchases were less in 2008 due to wood product facility curtailments and reduced purchases by CPLP.

## CANFOR WOOD RESIDUE UTILIZATION




Canfor is close to utilizing 100% of its wood products facility residuals.

## OCCUPATIONAL HEALTH AND SAFETY

Despite turbulent market conditions, Canfor's operations stayed true to the company's philosophy of "Safety Comes First at Canfor." In 2008, the Company continued the trend of improved safety performance towards a company-wide objective of a 2.0 Medical Incident Report (MIR) annual average, ending the year with a 2.72 MIR. The injury rate in our sawmills is less than half that of the rest of the industry.

Implementing initiatives that drove consistent best safety practices across the organization was a key focus for the year. Sharing of best practices between our operations, including safety plans, training, policy development and safety committee programs all contributed to the reduction in MIR.

The annual President's Safety Awards, in its 58th year, added two categories in order to better reflect the working conditions at certain sites. The awards recognize operating divisions for their exceptional health and safety performance. The winners of this year's President's Safety Awards produced impressive performance results, considering the very difficult operating environment. The 2008 award winners were Camden Sawmill for the lowest MIR; Vavenby Sawmill for the greatest percentage MIR improvement, 2007 to 2008; and the Rustad Sawmill for the lowest MIR for three consecutive years, 2006-2008.

The commitment all of our employees showed in 2008 and the results that they produced is proof of our unwavering focus on safety at the workplace.

# CORPORATE CITIZENSHIP

In 2008, the forest sector experienced a downturn of unprecedented magnitude. News from the industry was dominated by announcements of financial losses, market curtailments, and mill closures. Canfor maintained key commitments and long-term agreements, but reduced or eliminated some donations to reflect the challenging economic times.

Canfor's corporate giving focuses on the areas of youth and education, community enhancement, forestry and environment, amateur sport and health and wellness. The allocation of funding is coordinated through Canfor's head office with consultation and input from local employees to ensure that spending is made to meet the specific needs of individual communities.

## FOCUS ON PARTNERSHIPS – UNITED WAY

Canfor took part in the United Way's annual campaign, raising money that funds various Member Agencies and Programs that ensure there are support systems in place for children, families, seniors and new Canadians.

Donations from Canfor employees in Northern BC exceeded last year's totals, despite adverse economic conditions. Canfor and its employees also participated in United Way campaigns in the Lower Mainland of BC, the Kootenays, Alberta, and South Carolina.

## FOCUS ON COMMUNITY ENHANCEMENT – CHARLES JAGO NORTHERN SPORTS CENTRE

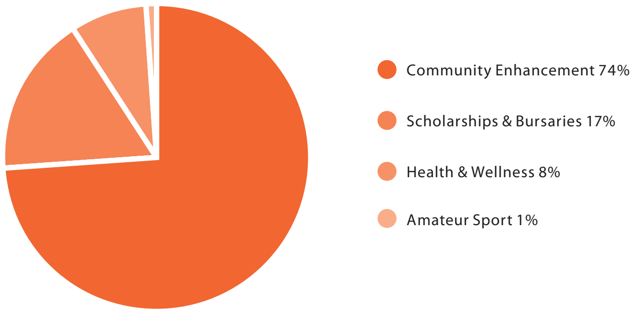
In 2008, Canfor was pleased to partner with the University of Northern British Columbia in the construction of the Charles Jago Northern Sports Centre. The 145,150 square foot facility sits at the entrance of the UNBC campus, providing training opportunities for high-performance athletes and much needed rental space for minor sport groups. In addition, the facility houses state-of-the-art fitness equipment available for public use through individual memberships.

Canfor partnered with the District of Houston in support of the new Aquatic Leisure Centre.

Canfor partnered with the District of Vanderhoof in support of its public library.

In 2008, Canfor proudly provided financial support to many diverse community groups, events and initiatives in our operating regions.

CORPORATE SUPPORT BY SEGMENT 2008



BELOW ARE JUST SOME OF THE ORGANIZATIONS WE HAVE SUPPORTED IN THE PAST

- BC Children's Hospital Foundation
- Houston – Aquatic & Leisure Facility
- Association of BC Forest Professionals
- STARS – Alberta Shock Trauma Rescue Society
- United Way of Lower Mainland
- Vanderhoof Public Library
- Prince George United Way
- VGH & UBC Hospital Foundation
- Quesnel & District Palliative Care Association
- Theatre Under The Stars
- Pacific Assistance Dog Society (PADS)
- Canadian Northern Children's Festival (Prince George)
- Theatre North West Society (Prince George)
- Prince George Public Library Reading Club
- Fort Nelson Fire Fighters
- Chilliwack Rugby Society
- Columbia Valley Gymnastics Association (Radium)
- Taylor Minor Hockey
- Crime Stoppers - Vavenby
- Mackenzie Moose Hockey Team
- Blue Lake Forest Education Society
- Myrtle Beach Chamber of Commerce – 2007 Canadian-American Days
- BC Sports Hall of Fame
- Chetwynd Youth Soccer Association
- Big Brothers / Big Sisters of Prince George
- United Native Nations Youth Hockey
- Aboriginal Business Development Centre
- Fort Nelson Trappers
- CIFAR
- Canadian Breast Cancer Foundation
- Junior Achievement of BC
- Girl Guides of Canada – Isle Pierre
- Chetwynd & District Minor Hockey
- Vanderhoof Air Cadets Squadron 899
- Prince George Chamber of Commerce
- Houtson Minor Hockey Association – 2007 Northern BC Winter Games
- Univeristy of Northern British Columbia
- University of British Columbia
- BCIT
- College of New Caledonia
- Northern Lights College

Please visit www.canfor.com/community to find out more about Canfor's community investment programs.

CANFOR

www.canfor.com