



**CANFOR CORPORATION  
Q2-2007 CONFERENCE CALL  
8am (Pacific) July 30, 2007**

**COMPANY REPRESENTATIVES**

**Jim Shepard – President and CEO**

**Scott Wilson – Vice –President, Finance and CFO**

**Don Kayne – Vice-President, Sales and Marketing**

**Operator:**

Good morning ladies and gentlemen. Welcome to the Canfor Corporation, second quarter result 2007 conference call. Please be advised that this call is being recorded at web cast live at [www.canfor.com](http://www.canfor.com). Our recoding of the call and the transcript will be available on Canfor's web site. Also the company would like to point out that this call will include forward-looking statements, so please refer to the press release for the associated risk of such statement. I would now like to turn the meeting over to Mr. Jim Shepard, President and CEO of Canfor Corporation. Please go ahead Mr. Shepard.

**Mr. Jim Shepard – President and CEO:**

Thank you and Good Morning everybody. I'm now going to give you the results of the second quarter. They were released on Friday. Just give you the highlights and then I'll give you some of my commentary. First, we reported the net loss of almost \$39 million or 27 cents of share in this quarter, as compared to a loss of \$43 million in the prior quarter. Despite higher prices for most of our products and improved operations during the second quarter, the strengthening of the Canadian dollar throughout the quarter made for another poor financial result for the quarter. From an operations perspective the mills ran well in the quarter of the five key metrics we measured – safety, productivity, recovery, cash, conversion cost and the percentage of prime rate out turns, all had modest improvements quarter over quarter. This reinforces our view that the deterioration of beetle killed wood in the harvested area such as Quesnel and Vanderhoof has plateaued and we're starting to understand how to handle the drier logs through the mills.

Now, if I may, I just like to stop and share with you my own experience here at Canfor which began just about three months ago. When I was asked to come in and serve as the interim CEO and President. When I arrived here, I knew that the first quarter result were not very good but the first month of the second quarter

were, were not looking any better and I called the executive together and on a team basis, we concluded that we would put together what we now call the "235 – 90" plan and basically that was the market condition at that time which we chose to use as where we're going to draw the line in the sand. What we considered to be the low of the cycle. We may have to adjust that, going forward but at this point of time as far as we're concerned, that is where we're going to operate and break even.

Now that's a lot easier said than done, but everything we've been doing from that day forward has been moving in the direction for a desired goal to be at [that point] by the time we get to the end of the year. Some initiatives that lead us to [here] was first of all, we started with a 25% payroll reduction. Now it's important to differentiate that between pay roll reduction and head count reduction. Other cost saving measures like this in the past have seen where the 25% was on the number of employees who were let go and quite often it was the people in the bottom part of the payroll that got let go and you aren't even getting an improved operation at all. Our 25% pay roll reduction covered all levels of the company. As a matter of fact it included the changing out of two of the Vice Presidents at the Executive level. One is the Vice President of Operations, which position is still open at the moment. But we are now actively recruiting and starting on the inside to find a replacement for that position and secondly Trevor James who was our VP of Human Recourses has, has now taken early retirement and Rob Stewart has stepped in, in his place. Other matters that, other measures that were complementary to that consistent with the 25% pay roll reduction. I gave myself a 25% pay reduction and I'm pleased to say that the board of directors got in the spirit of things and have voted themselves a 33% fee reduction.

We've also put out a cost reduction challenge to all of our vendors and all of our discussions with all vendors serving us at this time is concerning itself with how much they're going to reduce their cost to us in the coming year as opposed to the traditional kind of discussion where it was how much they're going to raise prices. That definitely is a lot of where Canfor is going forward for the foreseeable future. In addition to that we, we took the corporate jet out of service. It's a, it's a symbol, but it is a million dollar a year cost to us and quite frankly, I didn't think it's appropriate flying in to a community with a cooperate jet to announce that we were going to curtail or shut down a mill. If people can say well that's, that's just a visual in, in, it's just a symbol and that's true it is. But what we're trying to do here more than change the numbers, we're trying to change the attitudes and that's what the, that's where visuals and symbols come in and quite frankly, I do see and feel the attitude of this company is changing.

It started slowly, but I think it's picking up momentum now and I'm very, very enthusiastic about the kinds of results that this company is going to be able to deliver in the months and years ahead. One of the approaches that we're going to be taking with regard to getting our cost down, is getting better efficiency through the mills with regard to our grades and with regard to our cost of

conversion and we're seeing that is happening now, but basically what we're doing is we're going through a transition where we're treating all fourteen mills in British Columbia here as one factory, working with one system, delivering one product to one customer which is our marketing department, who's job it is to get the product to our customers on time and on tally and that's all – that, there's a constancy here, that's being built and quite frankly I think the prospects for our success in that area are very good.

I've been traveling as much as I can in the last three months to get as good a feel as I can as, as I came into this job as – some of you might know, my background was in heavy equipment with Finning and while we served Canfor, I never had any experience directly in the field of the forestry sector. So I've been traveling as fast as I can to learn as much as I can, but you could still fill the grand canyon of what I don't know about this business. So I'm probably stretching with some of my answers to your questions, but I'll do the best I can when we get to it. Any way, I think that's enough for now, for delivering remarks for now, passed the call on to Scott for some overall statements.

**Scott Wilson – Vice President of CFO:**

Okay. Thanks Jim. I won't take you through all the details of Friday's press release but will offer these comments. In the quarter Canfor generated sales of \$877 million, EBITDA of \$5 million and a net loss of \$39 million or 27 cents per share. A normal adjustment as listed on page four of our press release amount to 3 cent different. Therefore, the adjusted loss would have been 30 cents per share.

At the end of Q2 Canfor's net debt to capitalization was 5%, after we paid US\$ 10 million of long-term debt in the quarter. Will pay down a further US\$ 31.25 million in the third quarter. Canfor invested \$23 and a half million of capital in the second quarter. \$7.2 million relating to Canfor Pulp. This totals almost \$42 million for the year, of which \$32 million is for the wood products business. We now expect to spent in fact the lower end, of the \$100 to \$125 million in our wood product mills for the rest of the year. The Graham expansion project at New South is going well and is on budget and expected to start up on time in the last quarter of this year. At this point we have not developed plans for our 2008 capital program. At quarter end, Canfor had cash and temporary investments \$472 million on a consolidated basis.

Now to our business segments, beginning with lumber. EBITDA at negative \$28 million was an \$18 million improvement over the first quarter. The second quarter includes severance cost of \$4 million and a \$19 million favorable adjustment to the value of lumber inventory. In the first quarter there was a \$13 million write down of lumber inventory values. So the relative change quarter over quarter is \$32 million. As you've noted our mills are running well and we've seen modest quarter over quarter improvements of lumber recovery up, cash conversion cost

down, productivity up and a percentage of prime rates produced also up. Production from the SPF mills was 3% less this quarter than the previous quarter. Approximately 72 million board feet of production was lost primarily through market curtailments and we have announced 66 million board feet of market curtailments for the third quarter.

Shipments in the second quarter increased 12% from the first quarter and we continue to make progress to clear the back log of inventory built from the CN strike. As part of the BC ministry of forest annual review of the MPS stumpage formula, we expect base stumpage rates for Canfor's operations to be just under \$3 per cubic meter lower in Q3 than in Q2. Our New South mills also ran well in the quarter and contributed positive EBITDA.

Now looking at the panel segment. They had a \$2 million improvement in EBITDA in this quarter over the previous quarter, despite OSB prices in Canadian dollars being flat and plywood prices declining 6%; the improvement was driven by productivity improvement in the plywood mills which lowered conversion costs on a volumetric basis. Low production curtailments were taken in Q2. For Q3, the Tackama Plywood mill will take 8 and a half million square feet of production out for market reasons while Polar Board OSB, will take 14 million square feet production out.

And on the pulp and paper segment from last week's release of Canfor Pulp Limited Partnership's Q2 results you know, you know that despite strong operation and the 3% increase in US dollar list pulp prices, with 7% strengthening Canadian dollar and a 7% increase in chip prices, decreased Canfor Pulp's earnings to \$36 million from \$48 million in the previous quarter.

Although not included in Canfor's financials Howe Sound Pulp And Paper Ltd Partnership, earned \$7 million of EBITDA during the second quarter. The recapitalization program continues with expectations of completion by year end.

Before passing back to Jim, I'd like to thank David Jan for all of his efforts in supporting investor and analysts to understand Canfor. David is leaving the company and we all wish him well. Many of you know Pat Elliott, Canfor's Treasurer who will also assume the investor relations work going forward. Pat's contact info is included along with Lee Coonfer's for media support at the end of the news release. In addition Jim and I are always available to respond to your questions and with that Jim, I pass it to you.

**Mr. Jim Shepard – President and CEO:**

Thank you Scott. Well, consistent with our cost management plan, we now have a supply chain review on the way. We've got key people in from all parts of our operations. They've been working now for the last two weeks and basically what I - that is, is that they're working diligently to streamline the process, that's

involved from taking the lumber from the – from the rough inventory of the mill and delivering to the customers store. As you can appreciate there's a lot of logistics, a lot of systems and a lot of coordination that's required in there and we see tremendous opportunities for improvement. We had McKinsey, the consultants come in here earlier in the year and did a review of our operations and with their report indicated there was substantial savings to be achieved in this area and that's getting a lot of attention and that is all part of "235 – 90" cost reduction plan. Without any more commentary, I'll turn this meeting back over to the – to our coordinator here and open up the call for questions.

**Operator:**

Thank you. Will now take questions from the telephone line. We'll first take questions from the financial analysts, followed by the media. If you have a question, please press star one on your telephone keypad. If you're using a speakerphone, please lift the handset and then press star one. If at any time you wish to cancel your question please press the pound sign. Please press star one now, if you have a question. There will be a brief pause and participants will register the question. Thank you for your patients. The first question is from Don Roberts from CRBC world market. Please go ahead.

**Don Roberts – CIBC World Markets:**

Thank you. Jim first of all good luck. To start with, couple of questions first. In terms of you've now got this - this one hole of VP of Operations, are you considering in your organizational structure, especially given your talking about sort of 14 mills with one system or creating a **[COO position]** in here.

**Mr. Jim Shepard – President and CEO**

No, not at this time. We're talking about - something I failed to say is that, we've moved the VP of Operations position to Prince George, because the VP of Operation relates to VP of Canadian operations, because we now have a – an American operation as well, so at this point we are talking about VP Canadian operations located in Prince George.

**Don Roberts – CIBC World Markets:**

Okay. You – you'd already had some perspective of the company as a director before, but now that you've done sort of your visit in the operations, could you – I guess from your perspective identify the – I guess the one the biggest positive surprise you've found and then give us your biggest negative surprise.

**Mr. Jim Shepard – President and CEO**

The biggest positive surprise is – you know there is an expression that goes you know, the Hackney discussion has been set over and over again, where companies have said that people are a most important asset that's – I – I don't think that's true. I think what's true is the right people are your most important asset and what really surprised me and makes me most enthusiastic about this company is in my traveling to the 12 mills, three in the states and 9 here in British Colombia and also certainly visiting the people here in that office and all the meetings that we've gone through in getting this, this cost reduction plan on the way - is the, is the caliber of the people within Canfor. Quite frankly it was – it was, it was surprising and – and, and just, it really makes me enthusiastic about the prospects going forward.

Now and of course, in addition to that of course the – the, the, the, the fiber asset that we got as is a very valuable asset of course and then all the mill. The one that's – the most negative part let me see, I think probably, I guess the thing that concerns me most is how this company got off track in the last three years. Some of these major capital projects that were started, took a long, long time to get on the way and I just feel like there was a, I don't know – I get a sentiment lack of direction, when I got here and that's been part of the challenges of getting – getting that turned around, so we're all moving in the same direction, but I think that's coming along.

**Don Roberts – CIBC World Markets:**

Everyday underscores though, doesn't that this need that fill that operations position as soon as you can?

**Mr. Jim Shepard – President and CEO:**

Well, I guess it does, but on the other hand, we just had our board meeting on Friday and we have four regional managers there. Purposely I had all four regional managers come down and give their, and their presentation for their region and their participation in this "235 – 90" plan and I could honestly say to you, I was immensely proud of the presentation those four guys made. They stood shoulder to shoulder like the four musketeers and the board was very impressed as well and quiet frankly, I won't be a bit surprised if the VP of Operation comes out of – out of that group of very impressive individuals. So right to this moment, I haven't got a great concern about operations. I think these guys are absolutely given it and doing it in an excellent way.

**Don Roberts – CIBC World Markets:**

Okay. I mean, what are the distinctive features of the company's well being, your marketing strategy, you know the focus on the big box stress to some extent and yet in these kind of marketing conditions that we'll probably have to the end of

'08. As the – question is sort of, on your radar screen to do some of re-asses this marketing strategy and perhaps adapt something that's a little different.

**Mr. Jim Shepard – President and CEO:**

Okay. Well listen, I – my, my whole life is a marketing, so listen you already, always re-assessing your marketing strategy, the year your going to be going out of business. So that is constantly being challenged. But I did get an opportunity to travel south. With Don Kayne on one trip and another couple of trips on [indiscernible] but basic I did get a chance to visit with Centex and Valasue [ph], who build something like 35,000 homes a year. With - with Home Depot down the [indiscernible] and Charlet and with Malmin force products at St. Louis and Universal Forest Products and home build in Denver. So I've been working - and I understand that, that represent over 50% of our business. I think I got a fairly good flavoring of what's being said out there. Firstly, let me just say this. That, having the – the home center channel squarely in our sight and has been there for a while, where we devote the very strong position - a leadership position in that area, is immensely important in this kind of a market down turn and reminds me of depth like the – like what we had with Finning and here's what I'm talking about. Well, this down turn right now, your home construction market is falling off, tremendously. For one market that seems to be holding up better than anything else is the R&R market and that R&R market, goes through the home center. The home center channel to a large extent. So it's kind of like Finning, where our – where we have down turn, our new equipment sales fell off, but our part from service held up and I'm not it's exactly the same, but it reminds me of that. Quiet frankly I think that our strength is having that kind of channel to us - available to us and doing well at it and it's important to hold that channel together as we go through this down turn.

**Don Robert – CIBC World Markets:**

Okay. I could remember a more specific question, but I'll get back to you at the end of the queue. Thanks a lot.

**Operator:**

Thank You. The next question is from Sean Stueart from TD Newcrest. Please go ahead.

**Sean Stueart – TD Newcrest:**

Yep. Thank You. A couple of questions. I guess first for Scott. Maybe you can go through the inventory revaluation issue on lumber this quarter. I guess it was a \$19 million write up. Is that a great mix issue? I'm a bit surprised at the magnitude of that number.

**Scott Wilson – Vice President and CFO:**

No it's not Sean. It's a, just a, it's just a price issue and I know this has caused a little confusion, so I'll take you through the numbers. At the end of December, we had a devaluation balance of \$17.2 million. So at that time, they saw on our best estimate of future selling prices of lumber inventory. We believe that we would record a \$17 million loss on a ultimate sale of that inventory and the accounting rules require you to take that into your statement, till that period ends. So our devaluation balance at that point was \$17.2. At the end of the first quarter in March, we increased that devaluation balance by \$13 million. So an additional, assumed future loss. So the balance went to \$30 million and at the end of June, based on our best estimate of future selling prices at the end of the second quarter, we took \$19 million of that back, so that our devaluation balance at June 30<sup>th</sup> sits at a \$11 million and I should just re-emphasize that this our finished lumber only. There are no logs involved.

**Sean Stueart – TD Newcrest:**

Okay. That's helpful. And my – my second question is to you, Howe Sound. You mentioned I guess, capital restructuring expected by the end of the year. It seems to be stretched a little bit from the, the initial plan. Maybe some of the delays you're seeing there and - just curious on how much fiber, Howe Sound would have had before the strikes are placed, to get an idea of when you might be forced to curtail the mills?

**Scott Wilson – Vice President and CFO:**

Sure. First of all with respect to the overall restructuring, the Coastal strike has caused us to stand back a little bit, along with the Japanese banks and figure out how that could impact the cash flows that were assumed from Howe Sound for this year and what that means to the restructuring plan. So that – those discussions are on their way along with our partner Oji and that's going to delay what other ways, I think would have been a closing since restructuring, in and around this quarter, third quarter. As it relate to Howe Sound, fiber inventory, they're in pretty good shape. I think a lot of the coastal mills did prepare themselves as that possible and so something in the order of four to eight weeks of fiber inventory is there for them and they do have a little bit of options, between newsprint and the kraft mill and what they would be emphasizing, but there's no doubt, if that strike lasts beyond those time frames, I just mentioned that the mill will have to curtails and eventually shut.

**Sean Stueart – TD Newcrest:**

Okay. Thank you very much.

**Scott Wilson – Vice President and CFO:**

Okay Sean.

**Operator:**

Thank you. The next question is from Mark Bishop from RBC Capital Markets. Please go ahead.

**Mark Bishop - RBC Capital Markets:**

Oh, thanks. A couple of question. First Jim I, my apologies, I missed the very beginning of your call, but you're referring to, I think your cost reduction plan is "235 - 90" and again, if you elaborated on this at the beginning, I come back to that, but if not, could you elaborate on, on what exactly the "235 - 90" refers to?

**Mr. Jim Shepard - President and CEO:**

Yeah. The day that I - the day that I was appointed interim CEO which was the fourth of May, the market was at \$235 and the Canadian dollar was 90 cents and we, we chose that - to draw the line in the sand right there and then. That looked like it could be the low point of the cycle and what we're charged with was to stream line the operation and bring it up to an efficiency level that would enable us to run with that kind of a market at a break even and that's where we're at - that's what our target is by year end.

**Mark Bishop - RBC Capital Markets:**

Okay. Great. And just on that restructuring. On your US mill system - I'm not sure that we've heard of any cost reductions taken there. It seemed to me that when New South was acquired the administrative cost, effectively just stayed in tact including some very expensive senior management, which I understand is still an effective part of that organization, but were there any cost taken out of that part of the company.

**Mr. Jim Shepard - President and CEO:**

Yeah. Their, their - their certainly supporting the 235 - they should have and they're addressing exactly the same things we're addressing up here in Canada. They're running closer to the break even level than we are up here, so you know, there's three tightly net mills working together. It's a finely run organization quiet frankly, but there's certainly part of the team and there's certainly part of the spirit of getting themselves to the break even at the "235 - 90" and that is what we're considering as reality. We're ignoring the market as much as we can. If the market - I'd like, I'd gave you an example. When I first got here, after a couple of weeks, I would hear operations people say, "well see the market did pretty good last week" and it bothered me a lot to hear operations people talking about the

market, because quiet frankly, the market is not the focus you want of your operations people. Now with the problem with the market focus is that, is that if you – if you have your operations people like mill managers compensated on the basis of market realities, then basically what you do is, you allow them to celebrate achievements for which they have nothing, what so ever to do with and at the same, when the market goes into the tank, it becomes a catch all for a whole list of excuses why operations aren't any good and quiet frankly, I'd like to get market rate out of the vocabulary of operations people. In fact that it led me to – to introduce the five m's concept, which is met with a considerable amusement, but they get the point and that is the five m's is, we're going to mitigate the marketing mind set of our mill managers.

**Mark Bishop - RBC Capital Markets:**

Okay, great. Just turn it to stumpage; I think you'd indicated Scott that you are expecting to see a \$3 decline in stumpage, quarter over quarter. Is that correct?

**Scott Wilson – Vice President and CFO:**

Yeah. That's right.

**Mark Bishop - RBC Capital Markets:**

What component? Sorry.

**Scott Wilson – Vice President and CFO:**

Just under that.

**Mark Bishop - RBC Capital Markets:**

Just under that. What component of that is strictly the, you know the change I guess in the base rate in the new July rates in part I guess, influence by the option pricing and what is, I guess the influence of water bedding that you might have seen in a – can you break it out?

**Scott Wilson – Vice President and CFO:**

No. I'm afraid not. Pat may have some directions on that, to follow up on, but no.

**Mark Bishop - RBC Capital Markets:**

It's a little higher than we'd expected, so I was just curious to know what might have been driving that. The Mackenzie mill closure, I think there was an indication in your place that you were getting better access to fiber. I'm just wondering if you could elaborate on that and whether in fact that would have had

longer term support going back to the – or even in the newer term going back to the full capacity of Mackenzie.

**Mr. Jim Shepard – President and CEO:**

Let me, let me answer that one if I could. The Mackenzie, the announcement of the Mackenzie, indefinite shut down was part of the “235-90” plan. When we – when we rolled up ourselves here on the 7<sup>th</sup> of May, basically this company was, I mean to me it was like a patient coming into ER on life support and you know the first rule there is no matter what’s wrong you got to stop the bleeding. So we took a look and where we’re bleeding the most and it was Mackenzie. We were running at a rate of losing \$3 million a month. So we said okay, first thing we got to do is we got to stop that one and you know and quiet frankly, this business is got it’s, it’s got it, it’s got a numerous number of surprises to it. Not all of them are good, because what I found was that, it wasn’t as simple as just saying okay, well look, “let’s shut down Mackenzie until these markets improve and until we get our costs lined up or something” and it turned out that it wasn’t as easy as that, because – because the chip supply agreement, which were drafted a way back at a time I – I understand Fletcher Challenge were the – was the company that really got this, this agreement to be kind of like a, sort of a standard in the industry and basically what it is, is that there’s a force majeure clause, in those chips supply agreement, where as hard as the pulp mill was concerned the force measure has all the typical things like strike, riot, flooding, acts of god, but also it has the clause for economic conditions. So in other words, if the pulp market falls away, a pulp mill can phone up a saw mill and say “see, look. The markets fallen off. I don’t need your chips anymore.” On the other hand, it’s hard as far as the saw mill is concerned, there’s a force majeure clause, so the saw mill, if it has a riot or strike or any act of god, they can use the force majeure clause. But there’s nothing in there for economic conditions. So the fact that Mackenzie was running at a \$3 million a month loss was not good enough reason for us to tell our customers of our chips that we couldn’t supply them with chips. We are contractually obligated to supply those chips. So what our net was, at first glance it was “Well, good grief. We got to continue to operate Mackenzie and lose \$3 million every month, because we got to supply the chips.” Well, that wasn’t acceptable to us and we rolled up our sleeves and got working on it and we managed to do some creative things. One of the examples was our plant up in Fort St John [Taylor pulp mill], which we relied on hard wood and soft wood chips. What we did was, we put it over on pure hard wood chips, so we could draw a little soft wood chips away and ship them to our Mackenzie customers. We also made some, some, some changes down south. In other words to make a long story short we made the necessary adjustments and we’re going to be able to meet our chips supply contract with the indefinite shut down of Mackenzie and that was the direction we’re going in. I am very pleased to report that the response by all the interest of the parties has been very, very positive and I’m talking about the government, I’m talking about the city of Mackenzie, I’m talking about all the people that work at the Mackenzie mill and they’ve been working

hard with our management here over the last number of weeks to do whatever they can to assist us, enable us to keep this mill running and on the basis of that - that spirit of cooperation that's been shown by all the stake holders here, we decided that we're going to forego the indefinite shut down of Mackenzie, but we are going to and we're going to continue but running at with one mill instead of two mills. So there'll be a – a cut back in the production, but the mill will still continue to operate and still there's a substantial number of people employed and I think the reaction from the community up - there has been most positive and we will continue to – to perform and operate up there so as long as we can see that continuing cooperation.

**Mark Bishop - RBC Capital Markets:**

Oh that's – that's great. Just – just for clarification. Your chip supply agreement. Is it for volume at market or do you also have to take up any incremental transportation cost here to your account.

**Mr. Jim Shepard – President and CEO:**

I'm sorry. You mean when we are- you mean with regard supplying to our Mackenzie mill.

**Mark Bishop - RBC Capital Markets:**

Exactly.

**Mr. Jim Shepard – President and CEO:**

Yeah. No we where we going a have to - that was going to. What are the problems there was that we where going to have to take on incremental transportation cost to get those chips to the customer. That was all part of the bigger management that was involved there.

**Mark Bishop - RBC Capital Markets:**

Right okay. That's good, I've got other but I'll get in the queue. Thank you.

**Mr. Jim Shepard – President and CEO:**

Okay.

**Operation:**

Thank you the next question is from Paul Quinn from Salman Partners. Please go ahead.

**Paul Quinn – Salman Partners:**

Yeah, thanks. Just – just coming back to the Mackenzie decision. One of the things that I noticed in the market place was the - the lumber markets. What acted favorably to the down – down time announcement and because it was a large – large mill and production was coming off, do you – do you guys see now that – that additional curtailments are over required, given the market conditions or is – or is that not the case for Canfor.

**Mr. Jim Shepard – President and CEO:**

There will be addition curtailments where have needed, certainly and quite frankly that is happening on a – on a – on a focus basis thought the company with regard to - we got mills shutting down for a holiday, so we can get all the – get all the employees away on holidays at the same time and take some production out of the line. So we will continue to curtail as – as our competitors are doing. They are doing that as well.

**Paul Quinn – Salman Partners:**

Okay and this, in terms of your comments on the R&R market which is definitely a benefit to you guys. What percentage of Canfor's lumber is going into that market?

**Mr. Jim Shepard – President and CEO:**

Well listen I I'm going to plead ignorance because I'm not sure that I can even talk about that. Don Kayne is here and he's our marketing Vice President. Don you want to respond to that?

**Don Kayne –Vice President, Sales and Marketing:**

Oh, yeah Paul, the number continues to be around a fifth.

**Paul Quinn – Salman Partners:**

A fifth is going in R&R.

**Don Kayne –Vice President, Sales and Marketing:**

Right. And which has been pretty consistent for over years.

**Paul Quinn – Salman Partners:**

Okay.

**Don Kayne – Vice President, Sales and Marketing:**

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It hasn't gone up nor down. It's pretty flat based on our volume.

**Paul Quinn – Salman Partners:**

But in terms of the – the letters I guess you sent to all the vendors. What's it been the response in terms of try to get your supply cost down?

**Mr. Jim Shepard – President and CEO:**

Well it varies, it's been very – well I tell you what it is there's – there's, we had a couple of – we've had one supplier come back – the CEO came back right away and says "well give you the 15% and we asked for 15% as a – and we set that as the target as a challenge and one came back and said we'll meet that and we will hope that we'll be able to recover that from you when times are better, which was wonderful but that's a, that was an exception. What's it's really done is it's opened up a positive discussions with all of our major vendors about how they're going to – we're going to work with them and they're going to work with us to help us reduce our cost of taking delivery of what are their services or whatever their goods are and so it varies. We had a number of CEO's come back and had written back to me directly and it said that they've given instructions to the parts department to – to reduce the parts cost immediately and to talk - the sales department to open up the negotiations with outstanding quotations with us. So it varies from vender to vender, but the point is that they where all now discussing how much we're going to reduce the costs of Canfor and not how much we're going to raise the prices to Canfor.

**Paul Quinn – Salman Partners:**

Okay. So if I ask you to pick a number of what your cost reductions [will] yield, you'll, you'll - you expect to see - what can we use in our model?

**Mr. Jim Shepard – President and CEO:**

I really can't answer that right now, because it's just so variable at the moment and we've got so many discussions going on with so many of our vendors right now.

**Paul Quinn – Salman Partners:**

Okay.

**Mr. Jim Shepard – President and CEO:**

It's just to early quiet honest. We understand that, you know this – this “235 – 90” plan had really just got first of all, we got approval to move ahead on the 29<sup>th</sup> of may, so we had one month. The month of June with results, so we're really just getting started. The momentum is just picking up. But if my gut feel, tells me anything - it tells me that this momentum is gaining everyday.

**Paul Quinn – Salman Partners:**

Okay. Fare enough. I'll give you another quarter but just – just our last question.

**Mr. Jim Shepard – President and CEO:**

Yeah, give me. Okay, thank you.

**Paul Quinn – Salman Partners:**

But, just our last question. When you came in, many, many contacts in Canfor described you as an interim and you are classified as an interim no, no, no this guy is a board member and he's not the CEO. What changed to that?

**Mr. Jim Shepard – President and CEO:**

I'm sorry.

**Paul Quinn – Salman Partners:**

What - what changed since – since that perception to be nominated permanent president, CEO.- why did you take on this?

**Mr. Jim Shepard – President and CEO:**

Yeah, I ask – I ask me that question when I look in the mirror every morning. Well quite frankly, you know initially was the idea that I'd come in as interim CEO, but it was clearly understood that the – I mean this company needed direction. I mean that's for sure and I never came in as – as though I was – I didn't come in like I was a care taker and I'm just going to warm this seat until the permanent CEO arrives, you can't run a ship that way, so basically I came in and basically I walked in the door and I had responsibility that a chief executive had and I, and I told the Board that, that would be the way I approach it and they where perfectly comfortable with that and I have. The trouble is you got to be careful when you start something because you're going to be expected to finish it and that's basically where I'm at. We've had this thing as starting to come around and I think the Board feels and I can't disagree with them that it wouldn't be – it wouldn't be positive if we brought another CEO on board right now at this particular time and quite honestly, I must say I developed a very intense interest in this company and it's employees and it's customers. I think it's a tremendous

organization; I'm very enthusiastic about it and quite honestly it's – it's captured my imagination and I'm looking forward to being part of it for the foreseeable future.

**Paul Quinn – Salman Partners:**

Thanks

**Mr. Jim Shepard – President and CEO:**

Thank you.

**Operator:**

Thank you. Once again analyst please press star one if you have a question. The next question is from Don Roberts from CIBC World Market. Please go ahead.

**Don Roberts – CIBC World Markets:**

Thank you. This question is for Scott. Scott you may, I don't think you'd disclose it out right, but could you have some sense for the relatively even done margins between the New South operations and the Canadian ones. EBITDA in the south is also negative but can you give some sense for the relative difference?

**Scott Wilson – Vice President and CFO:**

Sure Don. The New South operations are – are actually positive, so I'm not going to say they real bad, but they're positive and in Canada with the SPF operations in Q2 our EBITDA margin was negative six.

**Don Roberts – CIBC World Markets:**

On 6%. Okay and back I guess, Jim had made some comments about, or may be it was you Scott, about the percent of prime rate actually up. I guess that surprises me some what given the beetle issues and so forth. Kind of [indiscernible] set up. Evidence suggest that things like J-grade is down. Could you give us in terms of where this is and tell me now, how sustainable this is?

**Mr. Jim Shepard – President and CEO:**

Don Kayne is probably going to answer this for you.

**Mr. Don Kayne – Vice-President, Sales and Marketing**

Plus we can, I think that over the second quarter I mean, I think that we're, just barely as result to some of the efforts that have been driven by the McKinsey

work, I think that Jim had referred to earlier. There's been a - an increase in focus for sure on the prime rates and it terms of our making sure that we're getting all the recovery that we can get in some of those grades and so we've with the improvement that we've made at the mills combined with some of the opportunities we've seen in the market place and bare in mind also Don that we haven't see a really big issue at this point in terms of the amount of blue stain in some of the products. I think Japan has a bit of an impact, but still even on J grade we're getting - we're getting a larger percentage than we've been getting recently, so that's really a credit for that. It's really the mills and what they've been able to do in the last three months in terms of improving recovery for those types of products which are so essential going forward for us, so.

**Don Roberts – CIBC World Markets:**

What percent of the sales typically now would be in your premium grades now weather it would be J grade, MSR, square HSR.

Mr. Don Kayne – Vice-President, Sales and Marketing

Yeah, we're big on that. We've been running around the third on that and that again is the consistent number that we've been able to achieve on our regular bases.

**Don Roberts – CIBC World Markets:**

Okay. What are you saying right now with regard to the European market. There is a prudence that I picked up some absolute activity, so could you can you give us some color on that.

Mr. Don Kayne – Vice-President, Sales and Marketing

On sorry. I missed - on Europe.

**Don Roberts – CIBC World Markets:**

On Europe yeah.

Mr. Don Kayne – Vice-President, Sales and Marketing:

Yeah well certainly on Europe, we've started looking at that late last year in terms of the opportunity there as you know prices there have increased significantly and activity levels there have been really good. So what we looked at particular with prices being where they wear, they had started the years, you know Don pretty low. We felt that there's potentially an opportunity there to do small - some small very focused volume there, particularly in the UK and take advantage of that market there for timber frame housing and that's what we've been doing. We

began a trial in early April, for eight weeks to really understand that cause we haven't done that before to any degree and we completed that trial at the end of June and we went back on North America basically for the next two months on regular dimension, while we assess the acceptance for that in the market place and weather or not there is additional grades of from a metric stamp point that we may be wanting to produce in the future.

**Don Roberts – CIBC World Markets:**

Ok. And it looks like it right now it's a pretty strong market in the Mid East for sort of lower grade stuff. How - have you seen this as well? Can you term it as well how sustainable if it is if it has occurred?

Mr. Don Kayne – Vice-President, Sales and Marketing:

:

Yeah I think a little bit everywhere, that's common for certainly for the Middle East. We've doubled our volume this year over the last year all ready, but that's the same for every where, I mean lower grade now is you know pretty short supply around the world, so weather your talking about the Middle East, China, Taiwan where ever you typically sell that type of product. It's strong in a lot of different areas.

**Don Roberts – CIBC World Markets:**

Okay. Okay. Thank you.

**Operator:**

Thank you. The next question is from Pierre Lacroix from Desjardins Securities. Please go ahead.

**Pierre Lacroix – Desjardins Securities:**

Yes, thank you very much. Yeah we understand that your taking fair deal of time on the reduction of cost through the system. In the press release you mentioned that you are going to take advantage of good opportunities in the future so may be if we talk about these good opportunities given the new management in place, did you change any kind of strategy regarding to that in term of specific products and also with timing of that.

**Mr. Jim Shepard – President and CEO of Canfor Corporation:**

Okay then. Pierre - we want to make sure we understood your question.

**Pierre Lacroix – Desjardins Securities:**

This is about growth opportunities.

**Mr. Jim Shepard – President and CEO:**

Growth opportunities.

**Pierre Lacroix – Desjardins Securities:**

Yes

**Mr. Jim Shepard – President and CEO:**

Oh yes. Okay, okay. Well let me just - if I can just share with you my personal experience. I spent ten years as chief exec with Finning and basically thought the years that company for example in 1982, was the year that a huge down turn in the forestry sector here in British Columbia and because we are a major supplier, we are affected tremendously by that and that was the year that we went from 2400 employees down to 1200 employees and shut down five branches and that was reported well were, the comp - we were going out of business. We had customers calling us in a panic. So things were pretty grim that year and we were down sizing but that was the same year that we went to the UK and bought two UK dealerships and merged it into one company and that was the beginning of our international growth as - as, as, as a caterpillar dealership. In 1993 I was the chief executive and those - cause in 1992 we had a very difficult year in British Columbia and again we were down sizing, shut down a couple of branches and that was the year we went to Chile and bought the Chile and caterpillar dealership there which it was established the beach head which enabled Finning and years later to then go on and purchase the dealership for Argentina and Uruguay and Bolivia. What I'm saying here, this is that the most opportune time to grow is when the market is at its worst and the only way you can do that is if you got a strong balance sheet and you've got the right people in the right people and I'd say those ingredients are here perfectly in Canfor.

**Pierre Lacroix – Desjardins Securities:**

And where do you see the opportunities currently right now?

**Mr. Jim Shepard – President and CEO:**

Well certainly the opportunities are pretty obvious. I mean the south is obviously - US south is the area that has the fiber and certainly could have some opportunities going forward. I don't think that's a secret loss than any body.

**Pierre Lacroix – Desjardins Securities:**

Would you consider going overseas.

**Mr. Jim Shepard – President and CEO:**

Anything, and never say never. We're not going, but I don't want to get into any speculation about it this time, but we'll be open. My experience – and again we're all victims of our experience and so I – I can only go by my own knowledge here and my knowledge if - basically if you would develop and fine tune your core consistency - core competency to apply where it's world competitive, then geography is not a barrier and that what our focus for the "235 – 90" is basically is to hold ourselves to be as thought as anybody when it comes to the bottom of the cycle. We achieve that then I believe we can operate any where.

**Pierre Lacroix – Desjardins Securities:**

And in term of products what do you see is the best potential for you? Are you ready to grow in other kind of products which has always be and engineered wood products for example?

**Mr. Jim Shepard – President and CEO:**

That's all under consideration right now, our direction that way.

**Pierre Lacroix – Desjardins Securities:**

Okay, thank you very much for that.

**Mr. Jim Shepard – President and CEO:**

Okay.

**Operator:**

Thank you. We'll now take questions from the media. If you have a question please press star one at this time. The next question will be from Don Roberts from CIBC world market. Please go ahead

**Don Roberts – CIBC World Markets:**

Yes, quick - Just one follow up I guess on Pierre's query. I just wanted before - can you help me understand the establish track record for growing off shore when the domestic markets weak, but in your own mind do you see that you

essentially have to demonstrate I guess this operation excellence with your current base first part of doing that, that there's perhaps a little bit of a credibility issue that's going off before we get the home operation in shape

**Mr. Jim Shepard – President and CEO:**

Well quite frankly growth in it's self is not satisfactory, you have to have profitable growth, okay. And I probably understand that, but the thing is you got to be able to walk and chew gum at the same time and well we're going to be working and are working like the dickens to get the "235 – 90" plan in place and streamlining our operation the way I described it earlier in the talk today, you know opportunities come when they come and as long as we're moving in the right direction, then the opportunity is properly priced. It isn't something that will pass up.

**Don Roberts – CIBC World Markets:**

Okay good. Thank you.

**Mr. Jim Shepard – President and CEO:**

Okay.

**Operator:**

Thank you. Once again please press star one at this time if you have a question. There are no further questions. I would like to return the meeting back to Mr. Shepard.

**Mr. Jim Shepard – President and CEO:**

Okay. Well thank you very much everybody for joining us. We appreciate your interest and appreciate your question and we look forward to getting back together again one quarter from now.

**Operator:**

Thank you. The conference is now ended. Please disconnect your lines at this time. We thank you for your participation and have a great day.