



FOR IMMEDIATE RELEASE

## CANFOR REPORTS RESULTS FOR FIRST QUARTER OF 2014

April 29, 2014 - Vancouver, B.C. - Canfor Corporation (TSX: CFP) today reported net income attributable to shareholders ("shareholder net income") of \$45.5 million, or \$0.33 per share, for the first quarter of 2014, compared to \$28.0 million, or \$0.20 per share, for the fourth quarter of 2013 and \$61.9 million, or \$0.43 per share, for the first quarter of 2013.

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

(millions of Canadian dollars, except per share amounts)	Q1 2014	Q4 2013	Q1 2013
Sales	\$ 741.9	\$ 809.5	\$ 786.3
Operating income, as reported	\$ 84.4	\$ 53.8	\$ 100.0
Operating income, adjusted for one-time items	\$ 84.4	\$ 74.9	\$ 100.0
Net income attributable to equity shareholders of the Company	\$ 45.5	\$ 28.0	\$ 61.9
Net income per share attributable to equity shareholders of the Company, basic and diluted	\$ 0.33	\$ 0.20	\$ 0.43
Adjusted shareholder net income	\$ 46.4	\$ 48.8	\$ 70.3
Adjusted shareholder net income per share, basic and diluted	\$ 0.34	\$ 0.35	\$ 0.49

After adjusting for items affecting comparability with the prior periods, the Company's adjusted shareholder net income for the first quarter of 2014 was \$46.4 million, or \$0.34 per share, compared to an adjusted shareholder net income of \$48.8 million, or \$0.35 per share, for the fourth quarter of 2013. Canfor's adjusted shareholder net income for the first quarter of 2013 was \$70.3 million, or \$0.49 per share.

The Company reported operating income of \$84.4 million for the first quarter of 2014, compared to operating income of \$53.8 million for the fourth quarter of 2013. After adjusting for one-time costs in the previous quarter, most notably costs associated with the announced closure of the Company's Quesnel Sawmill, operating income for the current quarter was up \$9.5 million. The modest improvement in operating income was largely attributable to gains in lumber and pulp sales realizations, with both benefitting from a weaker Canadian dollar. These gains were partially offset by significantly lower lumber and pulp shipments resulting from abnormally severe winter weather which limited railcar supply to Western Canada, and a 28-day truckers' strike at Canada's largest port in Vancouver, British Columbia.

The harsh winter weather conditions also curtailed home construction activity across much of North America in the current quarter. U.S. housing starts averaged 923,000 units SAAR (seasonally adjusted annual rate), down 8% from the previous quarter. In Canada, housing starts were down 11% from the fourth quarter of 2013, to 175,000 units SAAR. Offshore demand was stable but the truckers' strike at the port in Vancouver materially impacted lumber shipments.

The Company's lumber sales realizations in North America were up from the previous quarter, largely due to a 5% weaker Canadian dollar and, to a lesser extent, the absence of export taxes on U.S. bound shipments (for the Company's Canadian operations) compared to the previous quarter. U.S. dollar prices for North American products saw little change quarter-over-quarter, with a US\$3 decrease in the benchmark North American Random Lengths Western Spruce/Pine/Fir ("SPF") 2X4 #2&Btr price to US\$367 per Mfbm, offset by modest increases in several other grades and dimensions. Overall sales realizations for Southern Yellow Pine ("SYP") products saw modest increases compared to the previous quarter, with a US\$12 per Mfbm, or 3%, decrease in the benchmark SYP 2x4 #2 price, more than offset by moderate gains in wider dimension products. Offshore sales realizations (in US\$) saw moderate gains in the current quarter, for the most part reflecting stable demand and improved prices, the latter partly reflecting negotiated monthly or quarterly pricing.

Lumber shipments were down 16% from the previous quarter reflecting the aforementioned transportation challenges, while lumber production was up 3%, primarily the result of more operating hours mainly due to the Christmas period in the previous quarter as well as additional shifts in the current period at the Company's southern pine operations. Production in the current quarter continued to be impacted by capital related downtime and ramp-ups, as well as the closure of the Company's Quesnel Sawmill in mid-March. Unit manufacturing costs were higher compared to the previous quarter, reflecting a modest increase in unit log costs, principally driven by market-related increases in stumpage, coupled with higher seasonal and market-related energy costs and continued dust control efforts, all of which were partly offset by the favourable impact on unit costs from higher production.

Global softwood pulp markets showed a modest improvement in all major regions in the first quarter of 2014, while global softwood pulp producer inventory levels remained balanced over the period, increasing 1 day from the end of December 2013, to 28 days' supply in March 2014. Average Northern Bleached Softwood Kraft ("NBSK") pulp list prices saw solid gains in all regions during the first quarter of 2014, with the North American NBSK pulp list price increasing US\$34, or 3%, from the previous quarter to US\$1,017 per tonne (the highest level in almost three years), while list prices to China and Europe saw gains of 2%. Current quarter pulp sales realizations were also buoyed by the weaker Canadian dollar and proportionately higher shipments to the higher-margin U.S. market.

Pulp shipments were down 74,000 tonnes, or 22%, from the prior quarter, largely reflecting the transportation challenges experienced in the quarter. Pulp production levels were up 4% from the previous quarter, mainly as a result of an improvement in operating rates as the quarter progressed and a scheduled maintenance outage at Canfor Pulp's Prince George Pulp Mill in the previous quarter. Pulp unit manufacturing costs were up slightly compared to the previous quarter, with the favourable impact of increased production more than offset by higher market prices for sawmill residual chips and higher energy costs, the latter reflecting both seasonally higher consumption as well as natural gas price increases.

On March 28, 2014, the Company completed the sale of its Daaquam Sawmill. Total proceeds related to the disposition of the Daaquam operation approximated \$25 million.

Commenting on the first quarter performance, Canfor's President and Chief Executive Officer, Don Kayne, said, "Despite the many challenges presented by weather and transportation related disruptions, we continued to see progress during the quarter from the significant capital investments made at our lumber and pulp facilities in recent years."

Looking ahead, North American lumber consumption is forecast to rebound in the second quarter of 2014, as warmer weather contributes to stronger demand in the residential construction market. Lumber shipments across North America are anticipated to improve through the second and third quarters of 2014, releasing the backlog of shipments caused by the shortage of railcars earlier in 2014. Offshore lumber markets are projected to remain stable, supported by steady demand from Asia and other emerging markets. Delayed offshore lumber shipments resulting from the truckers' strike at the Vancouver Port are forecast to be largely cleared through the second quarter of 2014. NBSK pulp markets are projected to face challenges by the middle of the year; a risk of price weakness remains due in part to the significant new hardwood pulp capacity forecast to come online through 2014. Canfor Pulp anticipates that it will clear its transportation-related backlog of finished inventories by early in the third quarter of 2014.

#### **Additional Information and Conference Call**

A conference call to discuss the first quarter's financial and operating results will be held on Thursday, May 1, 2014 at 8:00 AM Pacific time. To participate in the call, please dial 416-340-9534 or Toll-Free 800-952-6845. For instant replay access until May 15, 2014, please dial 800-408-3053 and enter participant pass code 6959461#. The conference call will be webcast live and will be available at [www.canfor.com](http://www.canfor.com). This news release, the attached financial statements and a presentation used during the conference call can be accessed via the Company's website at <http://www.canfor.com/investor-relations/webcasts>.

## **Forward Looking Statements**

Certain statements in this press release 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.

*Canfor is a leading integrated forest products company based in Vancouver, British Columbia (“BC”) with interests in BC, Alberta, North and South Carolina and Alabama. Canfor produces primarily softwood lumber, and also produces bleached chemi-thermo mechanical pulp and specialized wood products. Canfor also owns a 50.4% interest in Canfor Pulp Products Inc., which is one of the largest producers of northern bleached softwood kraft pulp in Canada and a leading producer of high performance kraft paper. Canfor shares are traded on the Toronto Stock Exchange under the symbol CFP.*

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**Canfor Corporation**  
**First Quarter 2014**  
**Management's Discussion and Analysis**

*This interim Management's Discussion and Analysis ("MD&A") provides a review of Canfor Corporation's ("Canfor" or "the Company") financial performance for the quarter ended March 31, 2014 relative to the quarters ended December 31, 2013 and March 31, 2013, and the financial position of the Company at March 31, 2014. It should be read in conjunction with Canfor's unaudited interim consolidated financial statements and accompanying notes for the quarters ended March 31, 2014 and 2013, as well as the 2013 annual MD&A and the 2013 audited consolidated financial statements and notes thereto, which are included in Canfor's Annual Report for the year ended December 31, 2013 (available at [www.canfor.com](http://www.canfor.com)). The financial information in this interim MD&A has been prepared in accordance with International Financial Reporting Standards ("IFRS"), which is the required reporting framework for Canadian publicly accountable enterprises.*

*Throughout this discussion, reference is made to Operating Income before Amortization which Canfor considers to be a relevant indicator for measuring trends in the performance of each of its operating segments and the Company's ability to generate funds to meet its debt repayment and capital expenditure requirements. Reference is also made to Adjusted Shareholder Net Income (Loss) (calculated as Shareholder Net Income (Loss) less specific items affecting comparability with prior periods – for the full calculation, see reconciliation included in the section "Analysis of Specific Material Items Affecting Comparability of Shareholder Net Income (Loss)") and Adjusted Shareholder Net Income (Loss) per Share (calculated as Adjusted Shareholder Net Income (Loss) divided by the weighted average number of shares outstanding during the period). Operating Income before Amortization and Adjusted Shareholder Net Income (Loss) and Adjusted Shareholder Net Income (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 IFRS. As there is no standardized method of calculating these measures, Canfor's Operating Income before Amortization, Adjusted Shareholder Net Income (Loss) and Adjusted Shareholder Net Income (Loss) per Share may not be directly comparable with similarly titled measures used by other companies. Reconciliations of Operating Income before Amortization to Operating Income (Loss) and Adjusted Shareholder Net Income (Loss) to Net Income (Loss) reported in accordance with IFRS are included in this MD&A.*

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

*All financial references are in millions of Canadian dollars unless otherwise noted. The information in this report is as at April 29, 2014.*

**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.*

## FIRST QUARTER 2014 OVERVIEW

### Selected Financial Information and Statistics

(millions of Canadian dollars, except per share amounts)	Q1 2014	Q4 2013	Q1 2013
Operating income (loss) by segment:			
Lumber	\$ 56.4	\$ 37.4	\$ 88.4
Pulp and Paper	\$ 36.5	\$ 23.2	\$ 18.9
Unallocated and Other	\$ (8.5)	\$ (6.8)	\$ (7.3)
<b>Total operating income</b>	<b>\$ 84.4</b>	<b>\$ 53.8</b>	<b>\$ 100.0</b>
Add: Amortization	\$ 44.5	\$ 44.9	\$ 46.9
<b>Total operating income before amortization</b>	<b>\$ 128.9</b>	<b>\$ 98.7</b>	<b>\$ 146.9</b>
Add (deduct):			
Working capital movements	\$ (177.8)	\$ (14.5)	\$ (94.5)
Defined benefit pension plan contributions	\$ (13.5)	\$ (14.0)	\$ (13.5)
Other operating cash flows, net <sup>1</sup>	\$ 12.3	\$ 28.6	\$ 17.1
<b>Cash from (used in) operating activities</b>	<b>\$ (50.1)</b>	<b>\$ 98.8</b>	<b>\$ 56.0</b>
Add (deduct):			
Finance expenses paid	\$ (2.8)	\$ (5.9)	\$ (2.5)
Distributions paid to non-controlling interests	\$ (2.1)	\$ (2.4)	\$ (2.4)
Capital additions, net	\$ (53.1)	\$ (67.5)	\$ (46.4)
Investment in Scotch & Gulf Lumber, LLC	\$ -	\$ (0.5)	\$ -
Loan to Scotch & Gulf Lumber, LLC	\$ 2.6	\$ 2.1	\$ -
Repayment of long-term debt, net	\$ -	\$ (66.6)	\$ -
Other, net	\$ (2.9)	\$ (33.0)	\$ 5.6
<b>Change in cash / operating loans</b>	<b>\$ (108.4)</b>	<b>\$ (75.0)</b>	<b>\$ 10.3</b>
Quarterly ROIC – Consolidated <sup>2</sup>	3.5%	2.0%	4.8%
<b>Average exchange rate (US\$ per C\$1.00)<sup>3</sup></b>	<b>\$ 0.906</b>	<b>\$ 0.953</b>	<b>\$ 0.991</b>

<sup>1</sup> Other operating cash flows in the fourth quarter of 2013 include a \$20.0 million accounting provision for the closure of the Company's Quesnel Sawmill. Further information on operating cash flows can be found in the Company's unaudited interim consolidated financial statements.

<sup>2</sup> Consolidated Return on Invested Capital ("ROIC") is equal to operating income/loss, plus realized gains/losses on derivatives, equity income/loss from joint venture and other income/expense, all net of minority interest, divided by the average invested capital during the period. Invested capital is equal to capital assets, plus long-term investments and net non-cash working capital, all excluding minority interest components.

<sup>3</sup> Source – Bank of Canada (average noon rate for the period).

## Analysis of Specific Material Items Affecting Comparability of Shareholder Net Income

After-tax impact, net of non-controlling interests (millions of Canadian dollars, except per share amounts)	<b>Q1 2014</b>	<b>Q4 2013</b>	<b>Q1 2013</b>
<b>Shareholder net income, as reported</b>	<b>\$ 45.5</b>	<b>\$ 28.0</b>	<b>\$ 61.9</b>
(Gain) loss on derivative financial instruments	\$ 2.1	\$ 0.1	\$ (2.2)
Gain on sale of Daaquam Sawmill	\$ (1.6)	\$ -	\$ -
Foreign exchange loss on long-term debt	\$ -	\$ 1.5	\$ 2.3
Mill closure provisions	\$ -	\$ 14.8	\$ -
One-time costs associated with collective agreements for the lumber business	\$ -	\$ 0.8	\$ -
Loss on sale of Canfor-LP OSB <sup>4</sup>	\$ 0.4	\$ 3.6	\$ -
Canfor's 50% interest in Canfor-LP OSB's income, net of tax <sup>4</sup>	\$ -	\$ -	\$ 8.3
Net impact of above items	<b>\$ 0.9</b>	<b>\$ 20.8</b>	<b>\$ 8.4</b>
<b>Adjusted shareholder net income</b>	<b>\$ 46.4</b>	<b>\$ 48.8</b>	<b>\$ 70.3</b>
<b>Shareholder net income per share (EPS), as reported</b>	<b>\$ 0.33</b>	<b>\$ 0.20</b>	<b>\$ 0.43</b>
Net impact of above items per share	\$ 0.01	\$ 0.15	\$ 0.06
<b>Adjusted shareholder net income per share</b>	<b>\$ 0.34</b>	<b>\$ 0.35</b>	<b>\$ 0.49</b>

<sup>4</sup> The Company completed the sale of its 50% share of the Canfor-LP OSB Limited Partnership ("Canfor-LP OSB") in the second quarter of 2013 and recorded a gain of \$33.4 million (after tax). As part of the sale, Canfor may receive additional annual consideration over a 3 year period, starting June 1, 2013, based on Peace Valley OSB's annual adjusted earnings before interest, tax, depreciation and amortization. An asset was recorded based on the fair value of this additional consideration and will be adjusted to current estimated fair value each reporting period. Based on the estimated fair value at March 31, 2014, a loss of \$0.4 million (after tax) was recorded in the first quarter of 2014.

The Company reported operating income of \$84.4 million for the first quarter of 2014, compared to operating income of \$53.8 million for the fourth quarter of 2013. After adjusting for one-time costs in the previous quarter, most notably costs associated with the announced closure of the Company's Quesnel Sawmill, operating income for the current quarter was up \$9.5 million. The modest improvement in operating income was largely attributable to gains in lumber and pulp sales realizations, with both benefitting from a weaker Canadian dollar. These gains were partially offset by significantly lower lumber and pulp shipments resulting from abnormally severe winter weather which limited railcar supply to Western Canada, and a 28-day truckers' strike at Canada's largest port in Vancouver, British Columbia.

The harsh winter weather conditions also curtailed home construction activity across much of North America in the current quarter. U.S. housing starts averaged 923,000 units SAAR (seasonally adjusted annual rate), down 8% from the previous quarter. In Canada, housing starts were down 11% from the fourth quarter of 2013, to 175,000 units SAAR. Offshore demand was stable but the truckers' strike at the port in Vancouver materially impacted lumber shipments.

The Company's lumber sales realizations in North America were up from the previous quarter, largely due to a 5% weaker Canadian dollar and, to a lesser extent, the absence of export taxes on U.S. bound shipments (for the Company's Canadian operations) compared to the previous quarter. U.S. dollar prices for North American products saw little change quarter-over-quarter, with a US\$3 decrease in the benchmark North American Random Lengths Western Spruce/Pine/Fir ("SPF") 2X4 #2&Btr price to US\$367 per Mfbm, offset by modest increases in several other grades and dimensions. Overall sales realizations for Southern Yellow Pine ("SYP") products saw modest increases compared to the previous quarter, with a US\$12 per Mfbm, or 3%, decrease in the benchmark SYP 2x4 #2 price, more than offset by moderate gains in wider dimension products. Offshore sales realizations (in US\$) saw moderate gains in the current quarter, for the most part reflecting stable demand and improved prices, the latter partly reflecting negotiated monthly or quarterly pricing.

Lumber shipments were down 16% from the previous quarter reflecting the aforementioned transportation challenges, while lumber production was up 3%, primarily the result of more operating hours mainly due to the Christmas period in the previous quarter as well as additional shifts in the current period at the Company's southern pine operations. Production in the current quarter continued to be impacted by capital related downtime and ramp-ups, as well as the closure of the Company's Quesnel Sawmill in mid-March. Unit manufacturing costs were higher compared to the previous quarter, reflecting a modest increase in unit log costs, principally driven by market-related increases in stumpage, coupled with higher seasonal and market-related energy costs and continued dust control efforts, all of which were partly offset by the favourable impact on unit costs from higher production.

Global softwood pulp markets showed a modest improvement in all major regions in the first quarter of 2014, while global softwood pulp producer inventory levels remained balanced over the period, increasing 1 day from the end of December 2013, to 28 days' supply in March 2014. Average Northern Bleached Softwood Kraft ("NBSK") pulp list prices saw solid gains in all regions during the first quarter of 2014, with the North American NBSK pulp list price increasing US\$34, or 3%, from the previous quarter to US\$1,017 per tonne (the highest level in almost three years), while list prices to China and Europe saw gains of 2%. Current quarter pulp sales realizations were also buoyed by the weaker Canadian dollar and proportionately higher shipments to the higher-margin U.S. market.

Pulp shipments were down 74,000 tonnes, or 22%, from the prior quarter, largely reflecting the transportation challenges experienced in the quarter. Pulp production levels were up 4% from the previous quarter, mainly as a result of an improvement in operating rates as the quarter progressed and a scheduled maintenance outage at Canfor Pulp's Prince George Pulp Mill in the previous quarter. Pulp unit manufacturing costs were up slightly compared to the previous quarter, with the favourable impact of increased production more than offset by higher market prices for sawmill residual chips and higher energy costs, the latter reflecting both seasonally higher consumption as well as natural gas price increases.

Compared to the first quarter of 2013, operating income was down \$15.6 million, with operating income down \$32.0 million in the lumber segment and up \$17.6 million in the pulp and paper segment. These results included the impact from reduced sales volumes mainly attributable to the aforementioned transportation challenges in the current quarter, offset in part by improved lumber and pulp sales realizations, primarily reflecting the favourable impact of a 9% weaker Canadian dollar. Unit manufacturing costs were up in both segments compared to the same period in 2013, in part reflecting lower production levels, as a result of capital project ramp-ups, and increased energy costs as well as higher costs for raw materials.

## OPERATING RESULTS BY BUSINESS SEGMENT

### Lumber

#### Selected Financial Information and Statistics – Lumber

(millions of Canadian dollars unless otherwise noted)	Q1 2014	Q4 2013	Q1 2013
Sales	\$ 495.7	\$ 533.7	\$ 542.3
Operating income before amortization	\$ 84.3	\$ 66.1	\$ 115.7
Operating income	\$ 56.4	\$ 37.4	\$ 88.4
Mill closure provisions	\$ -	\$ 20.0	\$ -
One-time costs associated with collective agreements	\$ -	\$ 1.1	\$ -
Operating income excluding unusual items	\$ 56.4	\$ 58.5	\$ 88.4
Average SPF 2x4 #2&Btr lumber price in US\$ <sup>5</sup>	\$ 367	\$ 370	\$ 391
Average SPF price in Cdn\$	\$ 405	\$ 388	\$ 395
Average SYP 2x4 #2 lumber price in US\$ <sup>6</sup>	\$ 403	\$ 415	\$ 452
Average SYP price in Cdn\$	\$ 445	\$ 436	\$ 456
U.S. housing starts (thousand units SAAR) <sup>7</sup>	923	1,008	957
Production – SPF lumber (MMfbm) <sup>8</sup>	980.8	944.8	1,026.6
Production – SYP lumber (MMfbm) <sup>8</sup>	135.4	135.3	131.1
Shipments – SPF lumber (MMfbm) <sup>9</sup>	779.4	961.1	963.3
Shipments – SYP lumber (MMfbm) <sup>9</sup>	143.2	142.4	122.4
Shipments – wholesale lumber (MMfbm)	4.8	5.7	7.1

<sup>5</sup> Western Spruce/Pine/Fir, per thousand board feet (Source – Random Lengths Publications, Inc.).

<sup>6</sup> Southern Yellow Pine, Eastside, per thousand board feet (Source – Random Lengths Publications, Inc.).

<sup>7</sup> Source – U.S. Census Bureau, seasonally adjusted annual rate ("SAAR").

<sup>8</sup> Excluding production of trim blocks.

<sup>9</sup> Canfor-produced lumber, including lumber purchased for remanufacture and excluding trim blocks.

## Overview

Operating income for the lumber segment was \$56.4 million for the first quarter of 2014, an increase of \$19.0 million compared to operating income of \$37.4 million in the previous quarter, and down \$32.0 million from operating income of \$88.4 million reported for the first quarter of 2013. Results in the lumber segment for the fourth quarter of 2013 were impacted by various unusual items including an expense of \$20.0 million related to the announced closure of the Quesnel Sawmill and one-time costs of \$1.1 million associated with new five year collective agreements ratified in the quarter. Excluding the impact of these unusual items, operating income for the lumber segment was down \$2.1 million from the fourth quarter of 2013.

The decrease in lumber segment earnings compared to the fourth quarter of 2013 largely reflected a 16% decrease in shipments, primarily the result of the aforementioned transportation challenges in the quarter. Mostly offsetting the impact of reduced shipments were gains in sales realizations, which benefitted from a 5% weaker Canadian dollar and, to a lesser degree, lower export taxes over the period, with no export taxes on U.S. bound shipments in the current quarter. Higher unit cash conversion costs, reflecting increased energy costs and continued dust control efforts, were offset in part by the favourable unit impact of more production in the current quarter, resulting mainly from more operating hours. A modest increase in unit log costs was primarily driven by market-related increases in stumpage as well as higher hauling and logging costs.

Compared to the first quarter of 2013, the reduced operating income was mostly attributable to the transportation disruptions. The impact of a 15% decrease in sales volumes was lessened by improved sales realizations which reflected a favourable foreign exchange impact, offset in part by lower U.S. dollar prices across most grades. Unit manufacturing costs were up compared to the same period in 2013, driven principally by increased log costs, reflecting market-related stumpage increases and higher hauling and logging costs. Also contributing to the higher unit manufacturing costs were higher weather-related and market-related energy costs and lower production volumes, for the most part reflecting capital ramp-ups and the closure of the Quesnel Sawmill in the current period.

## Markets

During the first quarter of 2014, the lumber market was significantly hampered by an unusually severe winter. Overall lumber demand weakened as U.S. housing starts averaged 923,000 units<sup>10</sup> SAAR, down 8% from the fourth quarter of 2013 and 4% lower than the same period in 2013. Single-family starts, which consume a larger proportion of lumber, also dropped 8% compared to the fourth quarter of 2013 to 605,000 units<sup>10</sup> SAAR. Demand in the repair and remodeling sector experienced a similar temporary decline due to the prolonged winter. Furthermore, the weather also limited railcar supply to Western Canada, resulting in delayed Western SPF lumber shipments across the North American continent.

In Canada, lumber consumption was lower than the previous quarter, as Canadian housing starts averaged 175,000 units<sup>11</sup> SAAR for the quarter, down 21,000 units, or 11%, compared to the fourth quarter of 2013 and in line with the same period in 2013.

Canfor's offshore lumber shipments were down compared to the previous quarter due to the shortage of railcar supply and the truckers' strike in March at the port in Vancouver, Canada, which was resolved at the end of the quarter.

## Sales

Sales for the lumber segment for the first quarter of 2014 were \$495.7 million, compared to \$533.7 million in the previous quarter and \$542.3 million in the first quarter of 2013, as higher sales realizations in the current period were more than offset by lower shipments. Total shipments in the first quarter of 2014, at 923 million board feet, were down 16% from the previous quarter, and down 15% from the same period in 2013, largely reflecting the transportation challenges. Current quarter sales also included higher residual fibre revenue compared to both periods in 2013 due primarily to higher residual prices (linked to NBSK sales realizations).

<sup>10</sup> U.S. Census Bureau

<sup>11</sup> CMHC – Canada Mortgage and Housing Corporation

Solid gains in North American sales realizations compared to the previous quarter principally reflected the favourable impact of the 5% weaker Canadian dollar (for the Company's Canadian operations) and to a lesser extent, the absence of export taxes on U.S. bound shipments in the current quarter. Overall, there was little change in U.S. dollar prices for North American products, with a US\$3 per Mfbm decrease in the benchmark North American Random Lengths Western SPF 2X4 #2&Btr price to US\$367 per Mfbm, offset by modest increases in several other grades and dimensions. Offshore sales realizations (in US\$) saw moderate gains in the current quarter largely due to the nature of pricing, much of which is negotiated monthly or quarterly in advance. Overall sales realizations for SYP products were up slightly compared to the previous quarter, with a US\$12 per Mfbm, or 3%, decrease in the benchmark SYP 2x4 #2 price, more than offset by moderate gains in the 2x6 #2 price and other wider dimension products.

Compared to the first quarter of 2013, sales realizations showed a moderate improvement despite a marginal decrease in benchmark prices, principally reflecting a favourable foreign exchange impact, as sales realizations for Canadian operations benefited from a 9 cent, or 9%, weaker Canadian dollar. The benchmark North American Random Lengths Western SPF 2x4 #2&Btr price was down US\$24 per Mfbm, or 6%, compared to the first quarter of 2013, with higher decreases seen for several other grades and dimension products, including 2x6 #2 products. The impact from lower North American prices were somewhat lessened by a more muted decrease in quarter-over-quarter offshore sales realizations (in US\$). SYP products saw more marked decreases, with the benchmark SYP 2X4 #2 price down US\$49 per Mfbm, or 11%, and larger decreases were seen in wider dimension products. There were no export taxes on U.S. bound shipments in either quarter.

Total residual fibre revenue was higher in the current quarter compared to the fourth quarter of 2013, mainly reflecting market-driven increases in sawmill residual chip prices and to a lesser degree, higher shipments. Compared to the first quarter of 2013, total residual fibre revenue was also up, with higher sawmill residual chip prices more than offsetting slightly lower shipments of sawmill residual chips.

#### Operations

Lumber production, at over 1.1 billion board feet, was up 3% from the previous quarter, reflecting more operating hours largely due to the Christmas period in the previous quarter as well as additional shifts at the Company's southern pine operations. Capital related downtime and ramp-ups impacted both the current quarter and the fourth quarter of 2013, with the completion of the Company's Houston planer upgrade in the current quarter and the ramp-up of its Mackenzie and Darlington major sawmill upgrade projects through both periods. Compared to the first quarter of 2013, lumber production was down 4%, with productivity and operating hours impacted by capital projects, offset in part by continued capital-driven productivity improvements. Production in the current quarter was also impacted by the closure of the Company's Quesnel Sawmill in mid-March, while productivity was also hampered by the particularly harsh winter weather.

Overall, the Company's lumber unit manufacturing costs were higher than the previous quarter, driven by a modest increase in unit log costs and a similar increase in unit cash conversion costs. The increase in unit cash conversion costs in part reflected increases in energy costs as well as continued dust control efforts partially mitigated by the favourable impact of higher production levels on unit costs. Higher log costs were primarily attributable to market-driven increases in stumpage as well as higher hauling and logging costs.

Compared to the first quarter of 2013, unit manufacturing costs were up, principally reflecting the market-related stumpage increases and upward pressure on hauling and logging costs, in part due to higher diesel prices. Contributing to the increased unit manufacturing costs were the lower production volumes reflecting the capital ramp-ups in the current period, the continuing dust control efforts and higher energy costs, both severe weather and market-related, as well as higher labour costs.

## Pulp and Paper

### Selected Financial Information and Statistics – Pulp and Paper<sup>12</sup>

(millions of Canadian dollars unless otherwise noted)	<b>Q1 2014</b>	<b>Q4 2013</b>	<b>Q1 2013</b>
Sales	\$ 246.2	\$ 275.8	\$ 243.5
Operating income before amortization	\$ 53.0	\$ 39.2	\$ 38.3
Operating income	\$ 36.5	\$ 23.2	\$ 18.9
Average pulp price delivered to U.S. – US\$ <sup>13</sup>	\$ 1,017	\$ 983	\$ 897
Average price in Cdn\$	\$ 1,122	\$ 1,032	\$ 905
Production – pulp (000 mt)	310.4	299.5	317.0
Production – paper (000 mt)	36.7	30.8	34.8
Shipments – pulp (000 mt)	255.9	329.5	308.2
Shipments – paper (000 mt)	31.3	31.1	35.0

<sup>12</sup> Includes the Taylor Pulp Mill and 100% of Canfor Pulp Products Inc., which is consolidated in Canfor's results. Pulp production and shipment volumes presented are for both NBSK and bleached chemi-thermo mechanical pulp ("BCTMP").

<sup>13</sup> Per tonne, NBSK pulp list price delivered to U.S. (Resource Information Systems, Inc.).

#### Overview

Operating income for the pulp and paper segment was \$36.5 million for the first quarter of 2014, up \$13.3 million from the previous quarter, and up \$17.6 million from the first quarter of 2013.

Improved pulp and paper segment results compared to the previous quarter reflected a moderate increase in pulp sales realizations, resulting from increases in NBSK pulp list prices and a weakening of the Canadian dollar, down 5% from the previous quarter. Offsetting these gains were reduced shipments due to the aforementioned transportation challenges experienced in the current quarter. While overall shipments were down, sales realizations benefitted from reduced volumes to lower-margin regions, principally China. Unit manufacturing costs were up slightly compared to the previous quarter, with higher fibre (linked to NBSK pulp sales realizations) and energy costs largely offset by higher production volumes, primarily the result of improved operating rates. The current quarter results also included increased energy revenue with the start-up of Canfor Pulp's recently upgraded Northwood Pulp Mill turbines.

Higher operating earnings compared to the first quarter of 2013 principally reflected the improved NBSK pulp markets, with strong gains in NBSK pulp list prices across all regions coupled with a 9% weaker Canadian dollar. Partially offsetting these gains were lower total shipments compared to the same period in 2013 which similarly reflected the transportation challenges experienced in the current quarter. Compared to the first quarter of 2013, higher unit manufacturing costs reflected higher market-based fibre and energy costs and lower production levels, offset in part by lower chemical costs.

#### Markets

Global softwood pulp markets showed a modest improvement in the first quarter of 2014, with solid increases in list prices across all regions through the quarter and global softwood pulp producer inventory levels remaining in the balanced range. Global softwood pulp producer inventory levels increased 1 day from the end of December 2013, to 28 days' supply in March 2014<sup>14</sup>, partly reflecting the aforementioned transportation disruptions. Market conditions are generally considered balanced when inventories are in the 27-30 days of supply range.

Global shipments of bleached softwood kraft pulp were down 3% in the first quarter of 2014 compared to the previous quarter and relatively flat compared to the same period in 2013<sup>15</sup>. The decrease in softwood pulp shipments compared to the fourth quarter of 2013 reflected decreases to almost all regions in part due to the transportation challenges experienced in North America.

<sup>14</sup> World 20 data is based on twenty producing countries representing 80% of world chemical market pulp capacity and is based on information compiled and prepared by the Pulp and Paper Products Council ("PPPC").

<sup>15</sup> As reported by PPPC statistics.

## Sales

The Company's pulp shipments in the first quarter of 2014 were 256,000 tonnes, a decrease of 74,000 tonnes, or 22%, from the previous quarter, and down 52,000 tonnes, or 17% from the same period in 2013, largely reflecting the transportation challenges in the current quarter. Shipments to China were well down from both comparative periods, with the decrease relative to the fourth quarter of 2013 in part reflecting strong buying late in 2013 and the traditional Chinese Lunar New Year holiday in the current quarter, offset in part by increased volumes to the U.S. Reduced shipments compared to the previous quarter also reflected a build in finished goods inventories to target levels following a significant drawdown related to the higher Chinese purchasing activity at the end of 2013.

Global softwood pulp markets saw solid price increases through the current quarter, with the North American NBSK pulp list price reaching the highest level in almost three years, increasing US\$34 per tonne to US\$1,017, an increase of 3% from the fourth quarter of 2013. NBSK pulp list prices to China and Europe experienced similar solid gains through the quarter, both up 2% from the previous quarter to US\$753 per tonne and US\$920 per tonne, respectively. Current quarter sales realizations further benefitted from the 5% weaker Canadian dollar as well as increased shipments to the higher-margin U.S. market. Current quarter sales included higher energy revenue with the start-up of the Company's upgraded Northwood Pulp Mill turbines combined with additional operating days reflecting a planned maintenance outage of the Prince George Pulp Mill turbine in the fourth quarter of 2013. Bleached chemi-thermo mechanical pulp ("BCTMP") average sales realizations showed a solid increase compared to the previous quarter reflecting the weaker Canadian dollar coupled with a marginal increase in market prices.

Compared to the first quarter of 2013, pulp sales realizations saw strong gains as a result of marked improvements in average pulp list prices in all regions and the 9% weaker Canadian dollar. The North American NBSK pulp list price increased US\$120 per tonne, or 13%. NBSK pulp list prices to Europe and China also experienced solid increases, both up 11% compared to the first quarter of 2013. Contributing to the improved NBSK pulp list prices were reduced volumes to lower-margin regions, principally China, which more than offset the impact of increased pressure on discounts in North American markets compared to the same period in 2013. Energy revenue was also up compared to the same period in 2013, principally attributable to the upgrades to the Northwood Pulp Mill turbines. BCTMP sales realizations were well up compared to the first quarter of 2013, also reflecting higher market pricing and the weaker Canadian dollar.

## Operations

Pulp production in the current quarter was 310,000 tonnes, an increase of 11,000 tonnes, or 4%, from the previous quarter, and a decrease of 7,000 tonnes, or 2%, compared to the first quarter of 2013. Increased production compared to the fourth quarter of 2013 reflected an improvement in operating rates as the quarter progressed. The previous quarter also included a scheduled maintenance outage at Canfor Pulp's Prince George Pulp Mill which resulted in reduced market pulp production of 4,000 tonnes. Compared to the first quarter of 2013, production levels were impacted by slightly lower operating rates and increased transfers of slush pulp to the paper segment in the current quarter.

Pulp unit manufacturing costs increased slightly from the previous quarter, with higher energy costs, reflecting market-related price increases as well as increased consumption in part due to the harsh weather in the quarter, as well as a modest increase in fibre costs offsetting the favourable impact of higher production levels and reduced chemical and (timing-based) maintenance spending. Higher fibre costs principally reflected a market-related increase in prices for sawmill residual chips, where prices are linked to NBSK pulp sales realizations, mitigated slightly by seasonal pricing adjustments.

Higher unit manufacturing costs compared to the first quarter of 2013 were primarily driven by increased fibre costs and to a lesser extent, higher energy costs and the impact of lower production levels, offset in part by reduced chemical costs. The increase in energy costs resulted mainly from increased rates and higher gas usage, in part related to increased electricity generation. Contributing to the higher fibre costs in the current quarter were higher prices for sawmill residual chips, reflecting increased market prices, coupled with higher prices for whole log chips, in part related to pressure on stumpage rates, offset in part by a small decrease in the proportion of the higher-cost whole log chips.

**Unallocated and Other Items**  
**Selected Financial Information**

(millions of Canadian dollars)	<b>Q1</b>	<b>Q4</b>	<b>Q1</b>
	<b>2014</b>	<b>2013</b>	<b>2013</b>
Operating loss of Panels operations <sup>16</sup>	\$ (1.3)	\$ (0.5)	\$ (0.7)
Corporate costs	\$ (7.2)	\$ (6.3)	\$ (6.6)
Finance expense, net	\$ (4.4)	\$ (6.4)	\$ (8.8)
Foreign exchange loss on long-term debt	\$ -	\$ (3.4)	\$ (3.8)
Gain (loss) on derivative financial instruments	\$ (3.5)	\$ (0.2)	\$ 3.3
Other income (expense), net	\$ 3.3	\$ (3.1)	\$ 1.7

<sup>16</sup> The Panels operations include the Company's PolarBoard oriented strand board ("OSB") plant, which is currently indefinitely idled and its Tackama plywood plant, which was closed in January 2012.

Corporate costs were \$7.2 million for the first quarter of 2014, up slightly from both comparative periods in 2013, in part reflecting higher incentive-based compensation costs.

Net finance expense for the first quarter of 2014 was \$4.4 million, down \$2.0 million from the fourth quarter of 2013 and down \$4.4 million from the first quarter of 2013. The decrease from both comparative periods principally reflected lower debt levels in both Canfor and Canfor Pulp in the current quarter coupled with lower employee future benefit net interest costs, due in part to the improved financial position of most of the Company's defined benefit plans. Finance expense for the first quarter of 2013 included refinancing costs incurred to extend the maturity of the Company's principal operating loan facility.

The Company uses a variety of derivative financial instruments as partial economic hedges against unfavourable changes in foreign exchange rates, energy costs, lumber prices, pulp prices and interest rates. In the first quarter of 2014, the Company recorded a net loss of \$3.5 million related to its derivative instruments, principally reflecting unrealized losses on US dollar foreign exchange collars and forward contracts as a result of the weakening of the Canadian dollar through the quarter, as well as realized and unrealized losses on interest rate swap instruments due to lower interest rates between the respective quarter ends.

The following table summarizes the gains (losses) on derivative financial instruments for the comparable periods:

(millions of Canadian dollars)	<b>Q1</b>	<b>Q4</b>	<b>Q1</b>
	<b>2014</b>	<b>2013</b>	<b>2013</b>
Foreign exchange collars and forward contracts	\$ (2.9)	\$ 0.3	\$ 1.4
Energy derivatives	\$ 0.2	\$ 0.1	\$ 0.1
Lumber futures	\$ 0.1	\$ 0.2	\$ 2.2
Pulp futures	\$ (0.3)	\$ (0.1)	\$ -
Interest rate swaps	\$ (0.6)	\$ (0.7)	\$ (0.4)
	\$ (3.5)	\$ (0.2)	\$ 3.3

Other income, net of \$3.3 million in the first quarter of 2014 included a pre-tax accounting gain of \$2.2 million related to the sale of the Daaquam Sawmill in Quebec (see further discussion in the "Sale of Daaquam Sawmill" section later in this document). The Company also recorded a \$0.6 million negative fair value adjustment to the Canfor-LP OSB contingent consideration asset, largely reflecting weaker forecast OSB prices offset by favourable forecast foreign exchange rates over the contingent consideration period. Also included in other income, net in the current quarter were foreign exchange gains on US dollar denominated working capital of \$3.7 million resulting from the weakening of the Canadian dollar relative to the US dollar over the course of the quarter.

## Other Comprehensive Income (Loss)

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

(millions of Canadian dollars)	Q1 2014	Q4 2013	Q1 2013
Foreign exchange translation differences for foreign operations	\$ 10.6	\$ 8.0	\$ 3.5
Defined benefit actuarial gains (losses), net of tax	\$ (24.3)	\$ 40.4	\$ 5.8
Other comprehensive income (loss), net of tax	\$ (13.7)	\$ 48.4	\$ 9.3

In the first quarter of 2014, the Company recorded an after-tax loss to the Statements of Other Comprehensive Income (Loss) of \$24.3 in relation to changes in the valuation of the Company's employee future benefit plans. The loss reflects a lower discount rate used to value the net retirement benefit obligations, offset in part by a modest return on plan assets. Defined benefit actuarial gains, net of taxes, were recorded in both the comparable periods, with an after-tax gain of \$40.4 million in the fourth quarter of 2013 and an after-tax gain of \$5.8 million in the first quarter of 2013.

In addition, the Company recorded a \$10.6 million of other comprehensive gain in the quarter for foreign exchange differences for foreign operations, reflecting favourable foreign exchange movements during the quarter. This compared to a foreign exchange translation gain of \$8.0 million in the previous quarter and \$3.5 million in the first quarter of 2013.

## SUMMARY OF FINANCIAL POSITION

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

(millions of Canadian dollars, except for ratios)	Q1 2014	Q4 2013	Q1 2013
Increase (decrease) in cash and cash equivalents	\$ (1.6)	\$ (0.4)	\$ 23.3
Operating activities	\$ (50.1)	\$ 98.8	\$ 56.0
Financing activities	\$ 99.9	\$ (33.8)	\$ 8.1
Investing activities	\$ (51.4)	\$ (65.4)	\$ (40.8)
Ratio of current assets to current liabilities	1.7 : 1	1.7 : 1	1.5 : 1
Net debt to capitalization	13.1%	8.0%	18.8%
Quarterly ROIC – Consolidated	3.5%	2.0%	4.8%
Quarterly ROCE – Canfor solid wood business <sup>17</sup>	2.7%	2.4%	5.6%

<sup>17</sup> Return on Capital Employed ("ROCE") for the Canfor solid wood business represents consolidated ROCE adjusted to remove the Company's interest in Canfor-LP OSB and pulp and paper operations, including CPPI and the Taylor Pulp Mill. Consolidated ROCE is equal to shareholder net income for the period plus finance expense, after tax, divided by the average capital employed during the period (which consists of current and long-term debt and operating loans, and shareholders' equity, less cash and temporary investments).

## Changes in Financial Position

Cash used in operating activities was \$50.1 million in the first quarter of 2014, compared to cash generated of \$98.8 million in the previous quarter and cash generated of \$56.0 million in the same quarter of 2013. The decrease in operating cash flows from both comparative periods principally reflected a seasonal log inventory build coupled with significantly higher finished lumber and pulp inventory levels due to the transportation challenges experienced in the current quarter. The increase in non-cash working capital balances of \$177.8 million was partially offset by higher cash earnings in the first quarter of 2014. In addition, the Company made income tax payments of \$11.8 million in the first quarter of 2014 compared to \$0.3 million in the fourth quarter of 2013, and income taxes recovered of \$0.5 million in the first quarter of 2013.

Cash generated from financing activities was \$99.9 million in the current quarter, compared to cash used of \$33.8 million in the previous quarter and cash generated of \$8.1 million in the first quarter of 2013. The previous quarter cash flows included repayment of CPPI's US\$110 million 6.41% interest rate debt and the completion of CPPI's \$50.0 million floating rate term debt financing. During the current quarter, Canfor purchased 196,400 common shares under its Normal Course Issuer Bid for \$5.0 million, of which \$2.0 million was paid during the quarter. This compares to the purchase of 1,474,600 common shares for \$33.4 million, all of which was paid in the fourth quarter of 2013 (see further discussion of the shares purchased under the Normal Course Issuer Bid in the following "Liquidity and Financial Requirements" section). During the current quarter, the Company paid \$2.8 million in finance costs, down from \$5.9 million paid in the previous quarter that included the final interest payment on CPPI's US\$110

million term debt. Compared to the first quarter of 2013, cash used for financing activities was up \$91.8 million principally reflecting a net draw on the Company's operating loan facility of \$106.8 million compared to a net draw of \$13.0 million in the same quarter of the previous year. At the end of the first quarter, Canfor had \$182.0 million outstanding on its operating loan facilities.

Cash used for investing activities was \$51.4 million in the current quarter, compared to \$65.4 million in the fourth quarter of 2013 and \$40.8 million in the first quarter of 2013. Cash used for capital additions was \$53.1 million, down \$14.4 million from the previous quarter and up \$6.7 million from same quarter in 2013. Cash paid for capital in the current quarter included capital projects at the Company's Mackenzie, Grande Prairie and Houston operations. In the pulp and paper segment, current quarter capital expenditures of \$10.1 million primarily related to Canfor Pulp's Northwood and Intercontinental Pulp Mills' turbine upgrades. Construction of the Northwood Pulp Mill turbines was substantially completed in 2013 and the facility commenced selling power in the current quarter. Completion of the upgrade to the Intercontinental Pulp Mill turbine is targeted for early 2015.

### **Liquidity and Financial Requirements**

At March 31, 2014, the Company on a consolidated basis had cash of \$87.9 million, \$182.0 million drawn on its operating loans, and an additional \$26.0 million reserved for several standby letters of credit. Total available undrawn operating loans were \$272.0 million.

Canfor has \$100.0 million of floating interest rate term debt, repayable in February 2017 and CPPI has \$50.0 million of floating interest rate term debt, repayable in November 2018.

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

The Company's consolidated net debt to total capitalization at the end of the first quarter of 2014 was 13.1%. For Canfor, excluding CPPI, net debt to capitalization at the end of the first quarter was 12.9%.

On March 5, 2014, the Company renewed its normal course issuer bid whereby it can purchase for cancellation up to 6,995,228 common shares or approximately 5% of its issued and outstanding common shares as of February 28, 2014. The renewed normal course issuer bid is set to expire on March 4, 2015. During the first quarter of 2014, Canfor purchased 196,400 common shares for \$5.0 million, of which \$2.0 million was paid in cash in the period.

### **Sale of Daaquam Sawmill**

On March 28, 2014, the Company completed the sale of its Daaquam Sawmill. Total proceeds related to the disposition of the Daaquam operation approximated \$25 million, all of which were received subsequent to period end. A pre-tax gain of \$2.2 million was recorded in the first quarter of 2014 in Other Income.

## **OUTLOOK**

### **Lumber**

For the second quarter of 2014, North American lumber consumption is forecast to rebound as warmer weather is projected to result in stronger demand in the residential construction market and increased home improvement projects. Shipments across North America are anticipated to improve through the second and third quarters of 2014, releasing the backlog of shipments caused by the shortage of railcars earlier in 2014. Offshore markets are projected to remain stable, supported by steady demand from Asia and other emerging markets. Delayed offshore shipments resulting from the truckers' strike at the port in Vancouver are forecast to be largely cleared through the second quarter of 2014.

## **Pulp and Paper**

NBSK pulp markets are projected to face challenges by the middle of the year, with the annual spring maintenance downtime providing some supply side relief in the second quarter of 2014. For the month of April 2014, the Company announced NBSK pulp list prices of US\$1,030 per tonne in North America, unchanged from March 2014, and list prices to China and Europe also remained unchanged. A risk of price weakness remains due in part to the significant new hardwood pulp capacity forecast to come online through 2014. The Company anticipates that it will clear its transportation-related backlog of finished inventories by early in the third quarter of 2014.

## **OUTSTANDING SHARES**

At April 29, 2014, there were 139,572,193 common shares outstanding.

## **CRITICAL ACCOUNTING ESTIMATES**

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

## **ACCOUNTING STANDARDS ISSUED AND NOT APPLIED**

In May 2011, the International Accounting Standards Board ("IASB") issued IFRS 9, *Financial Instruments*. The required adoption date for IFRS 9 has been deferred from the original date of January 1, 2015 and is currently under review by the IASB.

Further details of the new accounting Standard and the potential impact on Canfor can be found in the Company's Annual Report for the year ended December 31, 2013.

## **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

During the quarter ended March 31, 2014, there were no changes in the Company's internal controls over financial reporting that materially affected, or would be reasonably likely to materially affect, such controls.

## **RISKS AND UNCERTAINTIES**

A comprehensive discussion of risks and uncertainties is included in the Company's 2013 annual statutory reports which are available on [www.canfor.com](http://www.canfor.com) or [www.sedar.com](http://www.sedar.com).

## SELECTED QUARTERLY FINANCIAL INFORMATION

	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012	Q3 2012	Q2 2012
<b>Sales and income</b> (millions of Canadian dollars)								
Sales	\$ 741.9	\$ 809.5	\$ 755.9	\$ 843.2	\$ 786.3	\$ 700.3	\$ 663.7	\$ 685.0
Operating income	\$ 84.4	\$ 53.8	\$ 49.3	\$ 128.2	\$ 100.0	\$ 49.0	\$ 18.1	\$ 22.6
Net income	\$ 58.6	\$ 35.1	\$ 33.6	\$ 114.3	\$ 67.5	\$ 24.7	\$ 18.8	\$ 5.0
Shareholder net income	\$ 45.5	\$ 28.0	\$ 28.4	\$ 110.3	\$ 61.9	\$ 21.3	\$ 20.5	\$ 2.6
<b>Per common share</b> (Canadian dollars)								
Shareholder net income – basic and diluted	\$ 0.33	\$ 0.20	\$ 0.20	\$ 0.77	\$ 0.43	\$ 0.15	\$ 0.14	\$ 0.02
Book value <sup>18</sup>	\$ 10.05	\$ 9.82	\$ 9.47	\$ 9.25	\$ 8.29	\$ 7.79	\$ 7.65	\$ 7.64
<b>Statistics</b>								
Lumber shipments (MMfbm)	927	1,109	1,172	1,224	1,093	1,110	1,093	1,120
Pulp shipments (000 mt)	256	330	268	308	308	298	269	282
Average exchange rate – US\$/Cdn\$	\$ 0.906	\$ 0.953	\$ 0.963	\$ 0.977	\$ 0.991	\$ 1.009	\$ 1.005	\$ 0.990
Average Western SPF 2x4 #2&Btr lumber price (US\$)	\$ 367	\$ 370	\$ 328	\$ 335	\$ 391	\$ 335	\$ 300	\$ 295
Average SYP (East) 2x4 #2 lumber price (US\$)	\$ 403	\$ 415	\$ 393	\$ 392	\$ 452	\$ 386	\$ 322	\$ 325
Average NBSK pulp list price delivered to U.S. (US\$)	\$ 1,017	\$ 983	\$ 947	\$ 937	\$ 897	\$ 863	\$ 853	\$ 900

<sup>18</sup> Book value per common share is equal to shareholders' equity at the end of the period, divided by the number of common shares outstanding at the end of the period.

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

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

After-tax impact, net of non-controlling interests (millions of Canadian dollars, except for per share amounts)	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012	Q3 2012	Q2 2012
<b>Shareholder net income, as reported</b>	\$ 45.5	\$ 28.0	\$ 28.4	\$ 110.3	\$ 61.9	\$ 21.3	\$ 20.5	\$ 2.6
(Gain) loss on derivative financial instruments	\$ 2.1	\$ 0.1	\$ (2.2)	\$ 1.0	\$ (2.2)	\$ 6.5	\$ (4.4)	\$ 4.2
Gain on sale of Daaquam Sawmill	\$ (1.6)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
(Gain) loss on sale of Canfor-LP OSB	\$ 0.4	\$ 3.6	\$ 1.0	\$ (33.4)	\$ -	\$ -	\$ -	\$ -
Foreign exchange (gain) loss on long-term debt and investments, net	\$ -	\$ 1.5	\$ (1.0)	\$ 1.8	\$ 2.3	\$ 1.2	\$ (4.0)	\$ 2.4
Mill closure provisions	\$ -	\$ 14.8	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
One-time costs associated with collective agreements for the lumber business	\$ -	\$ 0.8	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Canfor's 50% interest in Canfor-LP OSB's income, net of tax	\$ -	\$ -	\$ -	\$ 3.8	\$ 8.3	\$ -	\$ -	\$ -
Change in substantively enacted tax rate	\$ -	\$ -	\$ -	\$ 4.2	\$ -	\$ -	\$ -	\$ -
Net gain on post retirement and pension plan amendments	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (8.7)	\$ -	\$ -
Restructuring charges for management changes	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1.5	\$ -
Net impact of above items	\$ 0.9	\$ 20.8	\$ (2.2)	\$ (22.6)	\$ 8.4	\$ (1.0)	\$ (6.9)	\$ 6.6
<b>Adjusted shareholder net income</b>	\$ 46.4	\$ 48.8	\$ 26.2	\$ 87.7	\$ 70.3	\$ 20.3	\$ 13.6	\$ 9.2
<b>Shareholder net income per share (EPS), as reported</b>	\$ 0.33	\$ 0.20	\$ 0.20	\$ 0.77	\$ 0.43	\$ 0.15	\$ 0.14	\$ 0.02
Net impact of above items per share	\$ 0.01	\$ 0.15	\$ (0.02)	\$ (0.16)	\$ 0.06	\$ (0.01)	\$ (0.05)	\$ 0.05
<b>Adjusted net income per share</b>	\$ 0.34	\$ 0.35	\$ 0.18	\$ 0.61	\$ 0.49	\$ 0.14	\$ 0.09	\$ 0.07

## Canfor Corporation Condensed Consolidated Balance Sheets

(millions of Canadian dollars, unaudited)	As at March 31, 2014	As at December 31, 2013
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 87.9	\$ 89.5
Accounts receivable - Trade	118.7	112.6
- Other	66.5	39.3
Inventories (Note 2)	647.6	471.9
Prepaid expenses and other assets	36.0	39.1
<b>Total current assets</b>	<b>956.7</b>	<b>752.4</b>
<b>Property, plant and equipment</b>	<b>1,152.0</b>	<b>1,151.9</b>
<b>Timber licenses</b>	<b>530.8</b>	<b>534.6</b>
<b>Goodwill and other intangible assets</b>	<b>99.5</b>	<b>93.5</b>
<b>Retirement benefit surplus (Note 5)</b>	<b>27.5</b>	<b>42.2</b>
<b>Long-term investments and other (Note 3)</b>	<b>112.4</b>	<b>112.5</b>
<b>Deferred income taxes, net</b>	<b>6.2</b>	<b>6.2</b>
<b>Total assets</b>	<b>\$ 2,885.1</b>	<b>\$ 2,693.3</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Operating loans (Note 4)	\$ 182.0	\$ 74.6
Accounts payable and accrued liabilities	347.5	321.8
Current portion of deferred reforestation obligations	43.9	44.1
<b>Total current liabilities</b>	<b>573.4</b>	<b>440.5</b>
<b>Long-term debt</b>	<b>153.3</b>	<b>153.1</b>
<b>Retirement benefit obligations (Note 5)</b>	<b>209.4</b>	<b>200.5</b>
<b>Deferred reforestation obligations</b>	<b>83.4</b>	<b>69.8</b>
<b>Other long-term liabilities</b>	<b>14.3</b>	<b>14.9</b>
<b>Deferred income taxes, net</b>	<b>216.1</b>	<b>217.1</b>
<b>Total liabilities</b>	<b>\$ 1,249.9</b>	<b>\$ 1,095.9</b>
<b>EQUITY</b>		
Share capital	\$ 1,102.2	\$ 1,103.7
Contributed surplus	31.9	31.9
Retained earnings	255.3	234.2
Accumulated foreign exchange translation differences	15.1	4.5
<b>Total equity attributable to equity holders of the Company</b>	<b>1,404.5</b>	<b>1,374.3</b>
Non-controlling interests	230.7	223.1
<b>Total equity</b>	<b>\$ 1,635.2</b>	<b>\$ 1,597.4</b>
<b>Total liabilities and equity</b>	<b>\$ 2,885.1</b>	<b>\$ 2,693.3</b>

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

APPROVED BY THE BOARD

*"R.S. Smith"*

Director, R.S. Smith

*"M.J. Korenberg"*

Director, M.J. Korenberg

**Canfor Corporation**  
**Condensed Consolidated Statements of Income**

(millions of Canadian dollars, except per share data, unaudited)	3 months ended March 31,	
	<b>2014</b>	2013
<b>Sales</b>	<b>\$ 741.9</b>	\$ 786.3
<b>Costs and expenses</b>		
Manufacturing and product costs	<b>478.7</b>	492.2
Freight and other distribution costs	<b>113.8</b>	129.4
Amortization	<b>44.5</b>	46.9
Selling and administration costs	<b>18.3</b>	16.3
Restructuring, mill closure and severance costs	<b>2.2</b>	1.5
	<b>657.5</b>	686.3
<b>Operating income</b>	<b>84.4</b>	100.0
Finance expense, net	<b>(4.4)</b>	(8.8)
Foreign exchange loss on long-term debt	-	(3.8)
Gain (loss) on derivative financial instruments (Note 6)	<b>(3.5)</b>	3.3
Other income, net	<b>3.3</b>	1.7
Net income before income taxes	<b>79.8</b>	92.4
Income tax expense (Note 7)	<b>(21.2)</b>	(24.9)
<b>Net income</b>	<b>\$ 58.6</b>	\$ 67.5
<b>Net income attributable to:</b>		
Equity shareholders of the Company	<b>\$ 45.5</b>	\$ 61.9
Non-controlling interests	<b>13.1</b>	5.6
<b>Net income</b>	<b>\$ 58.6</b>	\$ 67.5
<b>Net income per common share:</b> (in Canadian dollars)		
Attributable to equity shareholders of the Company		
- Basic and diluted (Note 8)	<b>\$ 0.33</b>	\$ 0.43

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

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

(millions of Canadian dollars, unaudited)	3 months ended March 31,	
	<b>2014</b>	2013
<b>Net income</b>	<b>\$ 58.6</b>	\$ 67.5
<b>Other comprehensive income (loss)</b>		
Items that will not be recycled through net income:		
Defined benefit plan actuarial gains (losses) (Note 5)	<b>(32.8)</b>	7.7
Income tax recovery (expense) on defined benefit actuarial gains (losses) (Note 7)	<b>8.5</b>	(1.9)
	<b>(24.3)</b>	5.8
Items that may be recycled through net income:		
Foreign exchange translation differences for foreign operations	<b>10.6</b>	3.5
Other comprehensive income (loss), net of tax	<b>(13.7)</b>	9.3
<b>Total comprehensive income</b>	<b>\$ 44.9</b>	\$ 76.8
<b>Total comprehensive income attributable to:</b>		
Equity shareholders of the Company	<b>\$ 35.2</b>	\$ 71.1
Non-controlling interests	<b>9.7</b>	5.7
<b>Total comprehensive income</b>	<b>\$ 44.9</b>	\$ 76.8

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

## Canfor Corporation

### Condensed Consolidated Statements of Changes in Equity

	3 months ended March 31,	
(millions of Canadian dollars, unaudited)	2014	2013
<b>Share capital</b>		
Balance at beginning of period	\$ 1,103.7	\$ 1,126.2
Share purchases (Note 8)	(1.5)	-
Balance at end of period	\$ 1,102.2	\$ 1,126.2
<b>Contributed surplus</b>		
Balance at beginning and end of period	\$ 31.9	\$ 31.9
<b>Retained earnings</b>		
Balance at beginning of period	\$ 234.2	\$ (35.1)
Net income attributable to equity shareholders of the Company	45.5	61.9
Defined benefit plan actuarial gains (losses), net of tax	(20.9)	5.7
Share purchases (Note 8)	(3.5)	-
Balance at end of period	\$ 255.3	\$ 32.5
<b>Accumulated foreign exchange translation differences</b>		
Balance at beginning of period	\$ 4.5	\$ (10.5)
Foreign exchange translation differences for foreign operations	10.6	3.5
Balance at end of period	\$ 15.1	\$ (7.0)
<b>Total equity attributable to equity holders of the Company</b>	<b>\$ 1,404.5</b>	<b>\$ 1,183.6</b>
<b>Non-controlling interests</b>		
Balance at beginning of period	\$ 223.1	\$ 199.4
Net income attributable to non-controlling interests	13.1	5.6
Defined benefit plan actuarial gains (losses) attributable to non-controlling interests, net of taxes	(3.4)	0.1
Distributions to non-controlling interests	(2.1)	(2.4)
Balance at end of period	\$ 230.7	\$ 202.7
<b>Total equity</b>	<b>\$ 1,635.2</b>	<b>\$ 1,386.3</b>

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

## Canfor Corporation

### Condensed Consolidated Statements of Cash Flows

(millions of Canadian dollars, unaudited)	3 months ended March 31,	
	2014	2013
<b>Cash generated from (used in):</b>		
<b>Operating activities</b>		
Net income	\$ 58.6	\$ 67.5
Items not affecting cash:		
Amortization	44.5	46.9
Income tax expense	21.2	24.9
Long-term portion of deferred reforestation obligations	13.4	14.1
Foreign exchange loss on long-term debt	-	3.8
Changes in mark-to-market value of derivative financial instruments	3.4	(5.3)
Employee future benefits	3.2	3.5
Net finance expense	4.4	8.8
Other, net	4.3	(0.7)
Defined benefit pension plan contributions	(13.5)	(13.5)
Income taxes recovered (paid), net	(11.8)	0.5
	<b>127.7</b>	150.5
Net change in non-cash working capital (Note 9)	<b>(177.8)</b>	(94.5)
	<b>(50.1)</b>	56.0
<b>Financing activities</b>		
Change in operating bank loans	106.8	13.0
Finance expenses paid	(2.8)	(2.5)
Share purchases (Note 8)	(2.0)	-
Cash distributions paid to non-controlling interests	(2.1)	(2.4)
	<b>99.9</b>	8.1
<b>Investing activities</b>		
Additions to property, plant and equipment and intangible assets, net	(53.1)	(46.4)
Loan repayment from Scotch & Gulf Lumber, LLC (Note 11)	2.6	-
Other, net	(0.9)	5.6
	<b>(51.4)</b>	(40.8)
<b>Increase (decrease) in cash and cash equivalents*</b>	<b>(1.6)</b>	23.3
Cash and cash equivalents at beginning of period*	89.5	(17.1)
<b>Cash and cash equivalents at end of period*</b>	<b>\$ 87.9</b>	<b>\$ 6.2</b>

\*Cash and cash equivalents include cash on hand less unrepresented cheques.

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

## Canfor Corporation

### Notes to the Condensed Consolidated Financial Statements

(unaudited, millions of Canadian dollars unless otherwise noted)

#### 1. Basis of Preparation

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

These financial statements do not include all of the disclosures required by International Financial Reporting Standards ("IFRS") for annual financial statements. Additional disclosures relevant to the understanding of these financial statements, including the accounting policies applied, can be found in the Company's Annual Report for the year ended December 31, 2013, available at [www.canfor.com](http://www.canfor.com) or [www.sedar.com](http://www.sedar.com).

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

The currency of presentation for these financial statements is the Canadian dollar.

#### **Accounting Standards Issued and Not Applied**

In May 2011, the International Accounting Standards Board ("IASB") issued IFRS 9, *Financial Instruments*. The required adoption date for IFRS 9 has been deferred from the original adoption date of January 1, 2015 and is currently under review by the IASB.

Further details of the new accounting Standard and potential impact on Canfor can be found in the Company's Annual Report for the year ended December 31, 2013.

#### 2. Inventories

(millions of Canadian dollars)	<b>As at March 31, 2014</b>	As at December 31, 2013
Logs	\$ 218.0	\$ 134.5
Finished products	319.0	222.3
Residual fibre	9.5	14.9
Processing materials and supplies	101.1	100.2
	<b>\$ 647.6</b>	<b>\$ 471.9</b>

#### 3. Long-Term Investments and Other

(millions of Canadian dollars)	<b>As at March 31, 2014</b>	As at December 31, 2013
Investments	\$ 53.7	\$ 53.8
Term loan to Scotch & Gulf Lumber, LLC (Note 11)	31.6	33.0
Contingent consideration (Note 12)	12.2	11.4
Other deposits, loans and advances	14.9	14.3
	<b>\$ 112.4</b>	<b>\$ 112.5</b>

Included in Long-Term Investments and Other is Canfor's initial 25% interest in Scotch & Gulf Lumber, LLC ("Scotch Gulf") and a term loan receivable from Scotch Gulf (Note 11). Investments also include the Company's 33.3% investment in Lakeland Mills Ltd. and Winton Global Lumber Ltd. The Company does not have significant influence with respect to this investment.

#### 4. Operating Loans

##### *Available Operating Loans*

(millions of Canadian dollars)	As at March 31, 2014	As at December 31, 2013
<b>Canfor (excluding CPPI)</b>		
Available Operating Loans:		
Total operating loans - Canfor (excluding CPPI)	\$ 350.0	\$ 350.0
Drawn	(177.0)	(64.0)
Letters of credit (principally unregistered pension plans)	(13.8)	(14.8)
<b>Total available operating loans - Canfor (excluding CPPI)</b>	<b>\$ 159.2</b>	<b>\$ 271.2</b>
<b>CPPI</b>		
Available Operating Loans:		
Operating loan facility	\$ 110.0	\$ 110.0
Facility for letters of credit related to energy agreements	20.0	20.0
<b>Total operating loans - CPPI</b>	<b>130.0</b>	<b>130.0</b>
Drawn	(5.0)	(10.6)
Energy letters of credit	(12.2)	(12.2)
<b>Total available operating loans - CPPI</b>	<b>\$ 112.8</b>	<b>\$ 107.2</b>
<b>Consolidated:</b>		
<b>Total operating loans</b>	<b>\$ 480.0</b>	<b>\$ 480.0</b>
<b>Total available operating loans</b>	<b>\$ 272.0</b>	<b>\$ 378.4</b>

Canfor's principal operating loans, excluding Canfor Pulp Products Inc. ("CPPI"), mature on February 28, 2018. Interest is payable at floating rates based on the lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin that varies with the Company's net debt to total capitalization ratio.

The terms of CPPI's operating loan facility include interest payable at floating rates that vary depending on the ratio of net debt to total capitalization and is based on lenders' Canadian prime rate, bankers acceptances, US dollar base rate or US dollar LIBOR rate, plus a margin. The maturity date of this facility is January 31, 2018.

Both Canfor's and CPPI's operating loan facilities have certain financial covenants that stipulate maximum net debt to total capitalization ratios and minimum net worth amounts based on shareholders' equity.

CPPI has a separate facility with a maturity date of June 30, 2015 to cover energy-related letters of credit. At March 31, 2014, \$9.4 million of energy-related letters of credit were covered under this facility with the balance of \$2.8 million covered under CPPI's general operating loan facility.

As at March 31, 2014, the Company and CPPI were in compliance with all covenants relating to their operating loans. Substantially all borrowings of CPPI (operating loans and long-term debt) are non-recourse to other entities within the Company.

#### 5. Employee Future Benefits

For the three months ended March 31, 2014, a loss of \$32.8 million (before tax) was recognized in other comprehensive income in relation to changes in the valuation of the Company's employee future benefit plans. The loss reflects a lower discount rate used to value the net retirement benefit obligations, offset in part by a modest return on plan assets. For the three months ended March 31, 2013, a gain of \$7.7 million (before tax) was recognized in other comprehensive income.

For the Company's defined benefit plans, a one percentage point increase in the discount rate used in calculating the actuarial estimate of future liabilities would decrease the accrued benefit obligation by an estimated \$78.1 million.

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

<b>Pension Benefit Plans</b>	
Discount rate	
March 31, 2014	<b>4.40%</b>
December 31, 2013	4.80%
March 31, 2013	4.10%
December 31, 2012	4.20%
<b>Other Benefit Plans</b>	
Discount rate	
March 31, 2014	<b>4.50%</b>
December 31, 2013	4.90%
March 31, 2013	4.30%
December 31, 2012	4.40%

## 6. Financial Instruments

Canfor's cash and cash equivalents, accounts receivable, other deposits, loans and advances, operating loans, accounts payable and accrued liabilities, and long-term debt are measured at amortized cost subsequent to initial measurement. At March 31, 2014, the fair value of the Company's long-term debt approximates its amortized cost of \$153.3 million (December 31, 2013 - \$153.1 million).

Derivative instruments are measured at fair value. IFRS 13, *Fair Value Measurement*, requires classification of financial instruments within a hierarchy that prioritizes the inputs to fair value measurement.

The three levels of the fair value hierarchy are:

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

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

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

The following table summarizes Canfor's financial instruments measured at fair value at March 31, 2014 and December 31, 2013, and shows the level within the fair value hierarchy in which they have been classified:

(millions of Canadian dollars)	Fair Value Hierarchy Level	<b>As at March 31, 2014</b>	As at December 31, 2013
<b>Financial assets measured at fair value</b>			
Derivative financial instruments – held for trading	Level 2	\$ 0.3	\$ 0.6
Royalty receivable – available for sale	Level 3	4.7	5.3
Contingent consideration – available for sale (Note 12)	Level 3	12.2	12.8
		<b>\$ 17.2</b>	<b>\$ 18.7</b>
<b>Financial liabilities measured at fair value</b>			
Derivative financial instruments – held for trading	Level 2	\$ 3.5	\$ 0.3
		<b>\$ 3.5</b>	<b>\$ 0.3</b>

The royalty receivable and contingent consideration are measured at fair value at each reporting period and are presented in Other Accounts Receivable and Long-Term Investments and Other on the consolidated balance sheet, depending on their respective liquidity. The fair value of the royalty receivable is determined by discounting future expected cash flows based on energy price assumptions and future sales volume assumptions until the termination of the royalty agreement in September 2015. The fair value of the contingent consideration is determined by discounting future expected cash flows based on forecast oriented strand board ("OSB") prices, sales volumes, foreign exchange rates and margins for the Peace Valley OSB operation (Note 12).

The Company uses a variety of derivative financial instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, lumber prices, pulp prices, energy costs, and floating interest rates on long-term debt.

At March 31, 2014, the fair value of derivative financial instruments was a net liability of \$3.2 million (December 31, 2013 - net asset of \$0.3 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 three month periods ended March 31, 2014 and 2013:

(millions of Canadian dollars)	3 months ended March 31,	
	<b>2014</b>	2013
Foreign exchange collars and forward contracts	\$ (2.9)	\$ 1.4
Energy derivatives	0.2	0.1
Lumber futures	0.1	2.2
Pulp futures	(0.3)	-
Interest rate swaps	(0.6)	(0.4)
	<b>\$ (3.5)</b>	<b>\$ 3.3</b>

## 7. Income Taxes

(millions of Canadian dollars)	3 months ended March 31,	
	<b>2014</b>	2013
Current	\$ (13.9)	\$ (5.2)
Deferred	(7.3)	(19.7)
Income tax expense	<b>\$ (21.2)</b>	<b>\$ (24.9)</b>

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

(millions of Canadian dollars)	3 months ended March 31,	
	<b>2014</b>	2013
Income tax expense at statutory rate 2014 - 26.0% (2013 - 25.0%)	\$ (20.7)	\$ (23.1)
Add (deduct):		
Non-taxable income related to non-controlling interests in limited partnerships	0.1	-
Entities with different income tax rates and other tax adjustments	(0.4)	(1.3)
Permanent difference from capital gains and losses and other non-deductible items	(0.2)	(0.5)
Income tax expense	<b>\$ (21.2)</b>	<b>\$ (24.9)</b>

In addition to the amounts recorded to net income, a tax recovery of \$8.5 million was recorded to other comprehensive income for the three month period ended March 31, 2014 (three months ended March 31, 2013 - expense of \$1.9 million) in relation to the actuarial gains (losses) on defined benefit employee compensation plans.

## 8. Earnings Per Share and Normal Course Issuer Bid

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

	3 months ended March 31,	
	<b>2014</b>	2013
Weighted average number of common shares	<b>139,894,792</b>	142,752,431

On March 5, 2014, the Company renewed its normal course issuer bid whereby it can purchase for cancellation up to 6,995,228 common shares or approximately 5% of its issued and outstanding common shares as of February 28, 2014. The renewed normal course issuer bid is set to expire on March 4, 2015. During the first quarter of 2014, Canfor purchased 196,400 common shares for \$5.0 million (an average of \$25.46 per common share), of which \$2.0 million was paid in the quarter and the balance paid in April 2014.

## 9. Net Change in Non-Cash Working Capital

(millions of Canadian dollars)	3 months ended March 31,	
	2014	2013
Accounts receivable	\$ (13.8)	\$ (48.1)
Inventories	(194.9)	(99.5)
Prepaid expenses and other assets	(2.2)	1.5
Accounts payable, accrued liabilities and current portion of deferred reforestation obligations	33.1	51.6
Net increase in non-cash working capital	\$ (177.8)	\$ (94.5)

## 10. Segment Information

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

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

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

(millions of Canadian dollars)	Lumber	Pulp & Paper	Unallocated & Other	Elimination Adjustment	Consolidated
<b>3 months ended March 31, 2014</b>					
Sales to external customers	\$ 495.7	246.2	-	-	\$ 741.9
Sales to other segments	\$ 35.5	-	-	(35.5)	\$ -
Operating income (loss)	\$ 56.4	36.5	(8.5)	-	\$ 84.4
Amortization	\$ 27.9	16.5	0.1	-	\$ 44.5
Capital expenditures <sup>1</sup>	\$ 39.6	10.1	3.4	-	\$ 53.1
Identifiable assets	\$ 1,920.0	782.0	183.1	-	\$ 2,885.1
3 months ended March 31, 2013					
Sales to external customers	\$ 542.3	243.5	0.5	-	\$ 786.3
Sales to other segments	\$ 31.2	-	-	(31.2)	\$ -
Operating income (loss)	\$ 88.4	18.9	(7.3)	-	\$ 100.0
Amortization	\$ 27.3	19.4	0.2	-	\$ 46.9
Capital expenditures <sup>1</sup>	\$ 38.0	7.0	1.4	-	\$ 46.4
Identifiable assets	\$ 1,692.6	777.3	144.7	-	\$ 2,614.6

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

## 11. Phased Purchase of Scotch & Gulf Lumber, LLC

On August 9, 2013, the Company completed the first phase of the purchase of Scotch Gulf for \$29.5 million, representing an initial 25% interest in Scotch Gulf, plus transaction closing costs and a proportionate share of working capital. Canfor's initial 25% interest will increase over a 3 year period to 33% after twelve months, 50% after eighteen months and 100% at the end of the term. Scotch Gulf has an option under the purchase agreement to accelerate the final closing of the phased purchase to a date earlier than August 2016 under certain conditions. The aggregate purchase price for Scotch Gulf is US\$80.0 million, plus working capital.

As part of the transaction, Scotch Gulf borrowed \$34.0 million from Canfor in the form of a term loan that will be repaid from the distribution of cash earnings over the course of the phased purchase agreement with any net outstanding amount at August 2016 applied against the final phase purchase price payment. The term loan has an interest rate equal to the floating rate on Canfor's principal operating loans plus 1.0% and is secured by Scotch Gulf's operating assets. At March 31, 2014, \$31.6 million was outstanding on the term loan receivable which is included in Long-Term Investments and Other on the balance sheet (Note 3).

## **12. Sale of Canfor-LP OSB Joint Venture**

On May 31, 2013, the Company completed the sale of its 50% share in Canfor-LP OSB, which owns the Peace Valley OSB mill, to Louisiana-Pacific Corporation ("LP") for cash proceeds of \$77.9 million including working capital. A pre-tax gain on sale of \$38.3 million was recorded in the second quarter of 2013 which included recognition of Canfor's share of the operating income for the first half of 2013.

As part of the sale, Canfor may receive additional annual consideration over a 3 year period, starting June 1, 2013, contingent on Peace Valley OSB's annual adjusted earnings before interest, tax, depreciation and amortization. At March 31, 2014, the fair value of the contingent consideration is \$12.2 million, and is presented in Long-Term Investments and Other (Note 3). During the first quarter of 2014, Canfor recognized a \$0.6 million negative fair value adjustment on the contingent consideration in other expense.

## **13. Sale of Daaquam Sawmill**

On March 28, 2014, the Company completed the sale of its Daaquam Sawmill. Total gross proceeds related to the disposition of the Daaquam operation approximated \$25.0 million, all of which were received subsequent to period end. A pre-tax gain of \$2.2 million was recorded in the first quarter of 2014 in Other Income.