

February 19, 2008

## **CANFOR PULP INCOME FUND ANNOUNCES FOURTH QUARTER 2007 RESULTS**

Vancouver, B.C. – Canfor Pulp Income Fund (the “Fund”) (TSX:CFX.UN) announced today its fourth quarter 2007 results as well as the results of Canfor Pulp Limited Partnership (the “Partnership”) in which the Fund has a 49.8% ownership.

The Partnership reported sales of \$215.1 million and net income of \$12.1 million, or \$0.17 per unit, for the quarter ended December 31, 2007. The impact of a stronger Canadian dollar during the quarter and increased manufacturing costs reduced the results when compared to the prior quarter sales of \$228.9 million and net income of \$33.2 million, or \$0.46 per unit. Although fibre costs were maintained at the prior quarter levels, manufacturing costs increased when compared to the third quarter due to the seasonal impact on energy costs and higher spending on maintenance costs. The fourth quarter 2007 results are lower than those in the same period a year ago, when sales were \$225.2 million with net income of \$44.8 million or \$0.63 per unit, primarily due to the impact of the stronger Canadian dollar and fibre costs, which more than offset increases in NBSK pulp list prices.

The Partnership generated adjusted distributable cash (defined as standardized distributable cash before changes in working capital and after provision for accrued capital expenditures) of \$13.6 million, or \$0.19 per unit, in the fourth quarter and \$139.4 million, or \$1.96 per unit, for the year ended December 31, 2007. Capital expenditures incurred were \$14.7 million in the quarter and \$ 31.9 million for the year. Fluctuations in working capital are financed through the Partnership’s accumulated cash and bank credit lines.

Based on the Partnership’s results, the Fund earned net income of \$8.7 million, or \$0.25 per Fund unit, in the fourth quarter of 2007, compared to net income of \$12.2 million, or \$0.56 per Fund unit, in the same quarter of 2006.

In the fourth quarter, the Partnership produced 261,400 tonnes bringing the year’s total to 1,175,900 tonnes, an annual production record, bettering the previous year’s record by more than 31,000 tonnes. This quarter production level was 4,300 tonnes below the third quarter due in part to additional scheduled maintenance down time – 1,700 tonnes – and also as a result of the onset of winter operating conditions.

Commenting on the results, Paul Richards, President and CEO of the Partnership said: “It was another solid operating quarter and a record breaking year, with the establishing of new annual production and safety performance records, strong focus on controllable costs and the highest level of net sales since 1995. These factors enabled us to mitigate the impact of the rapid rise in the Canadian dollar and the increased pressure through the year on fibre supply and fibre price related to sawmill curtailments precipitated by the slowdown in the U.S. housing market.”

Pulp prices in U.S. dollars have continued to increase during the quarter but not sufficiently to fully offset the impact of the stronger Canadian dollar against U.S. currency. List prices at the end of the quarter were US\$870 per tonne for delivery to the United States and Northern Europe. The NBSK pulp market is currently balanced, with curtailments and closures in the printing and writing paper sector in both North America and Europe, combined with price sensitivity in Asia being balanced by the threat of further curtailments and closures of pulp production due to fibre shortages and the impact of the strong Canadian dollar.

The Partnership announced the appointment of Terry D. Hodgins, CA as Chief Financial Officer and Secretary. Mr. Hodgins was appointed Interim Chief Financial Officer and Secretary on October 24, 2007.

The Fund also announced its cash distribution for the month of February of \$0.12 per Fund unit, to be paid on March 14, 2008 to unitholders of record at the close of business on February 29, 2008.

### **Additional Information**

A conference call to discuss the fourth quarter 2007 financial and operating results will be held on Wednesday, February 20 at 8:00 a.m. Pacific time.

To participate in the call, please dial 416-641-6127 or Toll-Free 1-866-542-4238. For instant replay access, please dial 416-695-5800 or Toll-Free 1-800-408-3053 and enter participant pass code 3248556. The conference call will be webcast live and will be available at [www.canforpulp.com/investors/webcasts.asp](http://www.canforpulp.com/investors/webcasts.asp).

This news release and the attached Management’s Discussion and Analysis (MD&A) and financial statements are available on the company’s website at [www.canforpulp.com](http://www.canforpulp.com).

**About Canfor Pulp Income Fund**

The Fund is an unincorporated, open-ended trust established under the laws of Ontario, created to indirectly acquire and hold an interest in the Canfor Pulp Limited Partnership. The Fund indirectly holds a 49.8% interest in the Partnership with Canadian Forest Products Ltd. (a subsidiary of Canfor Corporation) holding the remaining 50.2% interest in the Partnership.

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## **Canfor Pulp Income Fund and Canfor Pulp Limited Partnership Fourth Quarter 2007 Management's Discussion and Analysis**

*Canfor Pulp Income Fund (the Fund) earns income from its 49.8% indirect interest in Canfor Pulp Limited Partnership (the Partnership). The Fund accounts for its investment in the Partnership on the equity basis and does not consolidate the operations of the Partnership. In order for the Fund's unitholders to understand the results of operations, the unaudited interim consolidated financial statements with accompanying notes are presented for both the Fund and the Partnership. The Partnership did not have an operating business prior to July 1, 2006, and the comparative results prior to this date represent the northern bleached softwood kraft (NBSK) business of Canadian Forest Products Ltd., a subsidiary of Canfor Corporation (collectively Canfor), which the Partnership acquired on July 1, 2006. This Management's Discussion and Analysis (MD&A) provides a review of the significant developments that have impacted the Partnership's and the Fund's performance for the quarter ended December 31, 2007 relative to the same period in the prior year and relative to the previous quarter. This MD&A should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes as well as the annual MD&A and audited consolidated financial statements and notes which are included in the Fund's 2006 Annual Report. Additional information relating to the Fund and the Partnership, including the Fund's Annual Information Form (AIF) dated March 19, 2007, is available on SEDAR at [www.sedar.com](http://www.sedar.com) or at [www.canforpulp.com](http://www.canforpulp.com).*

*In this document, references are made to EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization and before other non-operating income and expenses) and adjusted distributable cash. The Partnership considers EBITDA to be an important indicator for identifying trends in the Partnership's performance and of the Partnership's ability to generate funds to meet its debt service, capital expenditure requirements and to make cash distributions to its partners. Adjusted distributable cash is a measure of cash flow used by management to determine level of cash distributions. EBITDA and adjusted distributable cash should not be considered as alternatives to net income or cash flow from operations as determined in accordance with Canadian generally accepted accounting principles. As there is no standardized method of calculating these measures, the Partnership's use of these terms may not be directly comparable with similarly titled measures used by other companies or income funds.*

*Calculations of EBITDA and adjusted distributable cash are provided in a schedule at the end of this MD&A.*

*In this MD&A, for all periods ending prior to July 1, 2006, and for all annual periods, the financial information presented for the Partnership represents its business on a carve out basis (continuity of interests) from Canfor, as if operated as a stand-alone partnership entity for the full periods. The financial information presented includes allocations of certain of Canfor's assets, liabilities and costs. The financial condition, results of operations and cash flows for these periods are not necessarily indicative of the financial condition, results of operations or cash flows that would have been incurred if the business was a separate legal entity.*

*The information in this report is as at February 19, 2008.*

### **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", "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. The risks and uncertainties are detailed from time to time in reports filed by the Fund with the securities regulatory authorities in all of the provinces and territories of Canada to which recipients of this press release are referred to for additional information concerning the Fund and Partnership, its prospects and uncertainties relating to the Fund and Partnership and its prospects. These statements are based on management's current expectations and beliefs and actual events or results may differ materially. New risk factors may arise from time to time and it is not possible for management to predict all of those risk factors or the extent to which any factor or combination of factors may cause actual results, performance and achievements of the Fund and Partnership to be materially different from those contained in forward-looking statements. The forward-looking statements are based on current information and expectations and the Fund and Partnership assume no obligation to update such information to reflect later events or developments, except as required by law.

Forward-looking statements in this MD&A include statements made under the following headings:

- "Outlook – Pulp" on page 11;
- "Outlook – Kraft Paper Markets" on page 12;
- "Changes in Financial Position" on page 14, the second paragraph under that heading;
- "Subsequent Event" on page 15; and

- "Standardized Distributable Cash and Cash Distributions" on page 19.

Material risk factors that could cause actual results to differ materially from the forward-looking statements contained in this MD&A include: general economic, market and business conditions; product selling prices; raw material and operating costs; exchange rates; changes in law and public policy; and opportunities available to or pursued by the Fund and Partnership. Additional information concerning these and other factors can be found in this MD&A under the headings "Risks and Uncertainties" for the Fund and Partnership.

## CANFOR PULP INCOME FUND

The Fund is an unincorporated open-ended trust established under the laws of Ontario on April 21, 2006, pursuant to the Fund Declaration. The principal head office of the Fund is located at 1700 West 75<sup>th</sup> Avenue, Vancouver, BC, Canada. The Fund has been established to acquire and hold, through a wholly owned trust, the Canfor Pulp Trust (the Trust), investments in Limited Partnership Units of the Partnership, and such other investments as the Trustees of the Fund may determine. The general partner of the Partnership is Canfor Pulp Holding Inc. (the General Partner) and each limited partner holds an ownership interest in the General Partner equal to its proportionate interest in the Partnership.

At February 19, 2008, there are a total of 35,493,542 Fund units issued and outstanding, and the Fund indirectly holds a total of 35,493,542 units of the Partnership, representing 49.8% of the Partnership and Canfor holds 35,776,483 Class B Exchangeable Limited Partnership Units, representing 50.2% of the Partnership.

Each unitholder participates pro-rata in any distributions from the Fund. Under present income tax legislation, income tax obligations related to the distributions of the Fund are the obligations of the unitholders and the Fund is only taxable on any amount not allocated to the unitholders.

## EQUITY INVESTMENT IN CANFOR PULP LIMITED PARTNERSHIP

The Fund's equity investment in the Partnership is as follows:

(thousands of dollars)	<b>12 months ended December 31, 2007</b>	6 months ended December 31, 2006
Balance, beginning of period	<b>289,490</b>	116,560
Accounting policy change – Partners' equity of the Partnership	<b>2,363</b>	-
Accounting policy change – Accumulated other comprehensive income of the Partnership	<b>(915)</b>	-
Issuance of Fund units for exchangeable Partnership units (November 30, 2006) – 21,239,537 Fund units	-	182,791
Equity in income of the Partnership	<b>64,643</b>	20,558
Equity interest in other comprehensive income of the Partnership	<b>1,185</b>	-
Distributions earned	<b>(65,308)</b>	(30,419)
Balance, end of period	<b>291,458</b>	289,490

## SELECTED QUARTERLY FUND FINANCIAL INFORMATION

(thousands of dollars, except per unit amounts, unaudited)	<b>Q4 2007</b>	Q3 2007	Q2 2007	Q1 2007	Q4 2006	Q3 2006
Equity income in Canfor Pulp Limited Partnership	<b>5,999</b>	16,541	17,900	24,203	12,184	8,374
Net income (loss) <sup>1</sup>	<b>8,703</b>	16,541	(21,437)	24,203	12,184	8,374
Net income (loss) per Fund unit	<b>\$0.25</b>	\$0.46	(\$0.60)	\$0.68	\$0.56	\$0.59
Distributions earned from the Partnership	<b>13,487</b>	19,167	17,747	14,907	24,147	6,272
Distributions declared to unitholders	<b>13,487</b>	19,167	17,747	14,907	24,147	6,272
Distributions declared per Fund unit	<b>\$0.38</b>	\$0.54	\$0.50	\$0.42	\$0.80	\$0.44

Note: <sup>1</sup> In the second quarter of 2007 the Fund recorded a non-cash future income tax charge of \$39.3 million to net income relating to the Fund's 49.8% ownership in the Partnership and based on temporary differences between the accounting and tax basis of the Partnership's assets and liabilities expected to reverse after January 1, 2011. A recovery reduced this liability in the fourth quarter by \$2.7 million based on updated estimates of the temporary differences.

## **OPERATING RESULTS AND LIQUIDITY**

For the quarter ended December 31, 2007, the Fund had net income of \$8.7 million, or \$0.25 per Fund unit, representing its share of the Partnership's earnings for the period. Distributions declared by the Partnership and accruing to the Fund were \$13.5 million of which \$4.3 million was receivable at December 31, 2007. Cash distributions received from the Partnership are the only source of liquidity for the Fund. The Fund's requirements for administrative services are minimal and are funded and expensed by the Partnership.

## **FUND DISTRIBUTIONS**

The Fund is entirely dependent on distributions from the Partnership to make its own distributions and declares distributions on a monthly basis with the record date on the last business day of each month and payable within the 15 days following. Distributions from the Fund's investment in the units of the Partnership and distributions payable by the Fund to its unitholders are recorded when declared. During the fourth quarter of 2007, the Fund declared distributions of \$0.38 per Fund unit or a total of \$13.5 million.

Monthly cash distributions from the Partnership are not directly equal to the Fund's pro-rata share of the Partnership's income under the equity method, primarily due to differences between capital expenditure amounts and amortization and other non-cash expenses of the Partnership.

## **RISKS AND UNCERTAINTIES**

The Fund is subject to certain risks and uncertainties related to the nature of its investment in the Partnership and the structure of the Fund, as well as all of the risks and uncertainties related to the business of the Partnership. A comprehensive discussion of these risks and uncertainties is contained in the Fund's Annual Information Form dated March 19, 2007, which is available on [www.sedar.com](http://www.sedar.com).

## **RELATED PARTY TRANSACTIONS**

All accounting, treasury, legal and administrative functions for the Fund are performed on its behalf by the Partnership pursuant to a support agreement. Distributions earned from the Partnership for the 3 months and year ended December 31, 2007 were \$13.5 million and \$65.3 million respectively, of which \$9.2 million and \$61.0 million were paid, with the balance of \$4.3 million receivable on December 31, 2007.

## **CRITICAL ACCOUNTING ESTIMATES**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements. Management regularly reviews these estimates and assumptions based on currently available information. The determination of the future income tax liability requires management to estimate the future impacts of amortization of capital assets, capital cost allowance claims for tax purposes and changes to actuarial estimates of employee benefit plans. Changes in these estimates could have a material impact on the calculation of the liability.

## **CHANGES IN ACCOUNTING POLICIES**

### *Future Income Taxes*

In June 2007 legislation was substantively enacted to tax distributions of publicly traded income trusts, commencing in 2011. As a result, the Fund is now required to recognize the future income tax assets and liabilities expected to arise when the tax on distributions becomes applicable.

Future income tax assets and liabilities are determined based on the difference between the tax basis of the Fund's pro-rata ownership of the Partnership's assets and liabilities and the respective amounts reported in the financial statements. Future tax assets or liabilities are calculated using the substantively enacted tax rates for the periods in which the differences are expected to be settled. Future tax assets are recognized to the extent that they are considered more likely than not to be realized.

## *Financial Instruments*

Effective January 1, 2007, the Fund adopted the Canadian Institute of Chartered Accountants' new Handbook Section 3855 "Financial Instruments – recognition and measurement" and Section 1530 "Comprehensive Income". These standards were adopted retroactively and comparative amounts of prior periods have not been restated.

Section 3855 prescribes when a financial instrument should be recognized on the balance sheet and at what amount. It also specifies how to present financial instrument gains and losses. Under Section 3855, all financial instruments are classified into one of these five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments and derivatives are measured in the Consolidated Balance Sheets at fair value on initial recognition except for certain related party transactions. Subsequent measurement depends on the initial classification of the instrument. Loans and receivables, held-to-maturity investments and other financial liabilities are measured at amortized cost. All derivative instruments, including embedded derivatives, are recorded in the Consolidated Balance Sheets at fair value unless they qualify for the normal sales and purchases exemption. Changes in the fair value of derivatives that are not exempt are recorded in income.

As a result of adopting these new standards, the Fund has classified its distribution receivable as loans and receivables. Distributions payable are classified as other liabilities and are measured at amortized cost.

Section 1530 introduces new requirements for situations when certain gains and losses ("other comprehensive income") must be temporarily presented outside of net income in a new Statement of Comprehensive Income. Comprehensive income is the change in the Fund's Unitholder's equity that result from transactions, events and circumstances from sources other than the Unitholders. For the period ended December 31, 2007, the Fund's other comprehensive income resulted from its equity interest in the Partnership (see note 3 to the consolidated financial statements of the Partnership).

### **NEW ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED**

The CICA has issued two new standards which may affect the financial disclosures and results of operations of the Fund for interim and annual periods beginning January 1, 2008. The Fund will adopt the requirements commencing in the interim period ended March 31, 2008 and is considering the impact this will have on the Fund's financial statements.

#### **1. Section 1535 – Capital Disclosures**

This Section establishes standards for disclosing information about an entity's capital and how it is managed. Under this standard the Fund will be required to disclose the following, based on the information provided internally to the Fund's key management personnel:

- (i) qualitative information about its objectives, policies and processes for managing capital;
- (ii) summary quantitative data about what it manages as capital;
- (iii) whether during the period it complied with any externally imposed capital requirements to which it is subject;
- (iv) when the Fund has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

#### **2. Section 3862 – Financial Instruments – Disclosures**

This Section requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the Fund is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks. The Fund will be required to disclose the measurement basis or bases used, and the criteria used to determine classification for different types of instruments.

The Section requires specific disclosures to be made, including the criteria for:

- (i) designating financial assets and liabilities as held for trading;
- (ii) designating financial assets as available-for-sale; and
- (iii) determining when impairment is recorded against the related financial asset or when an allowance account is used.

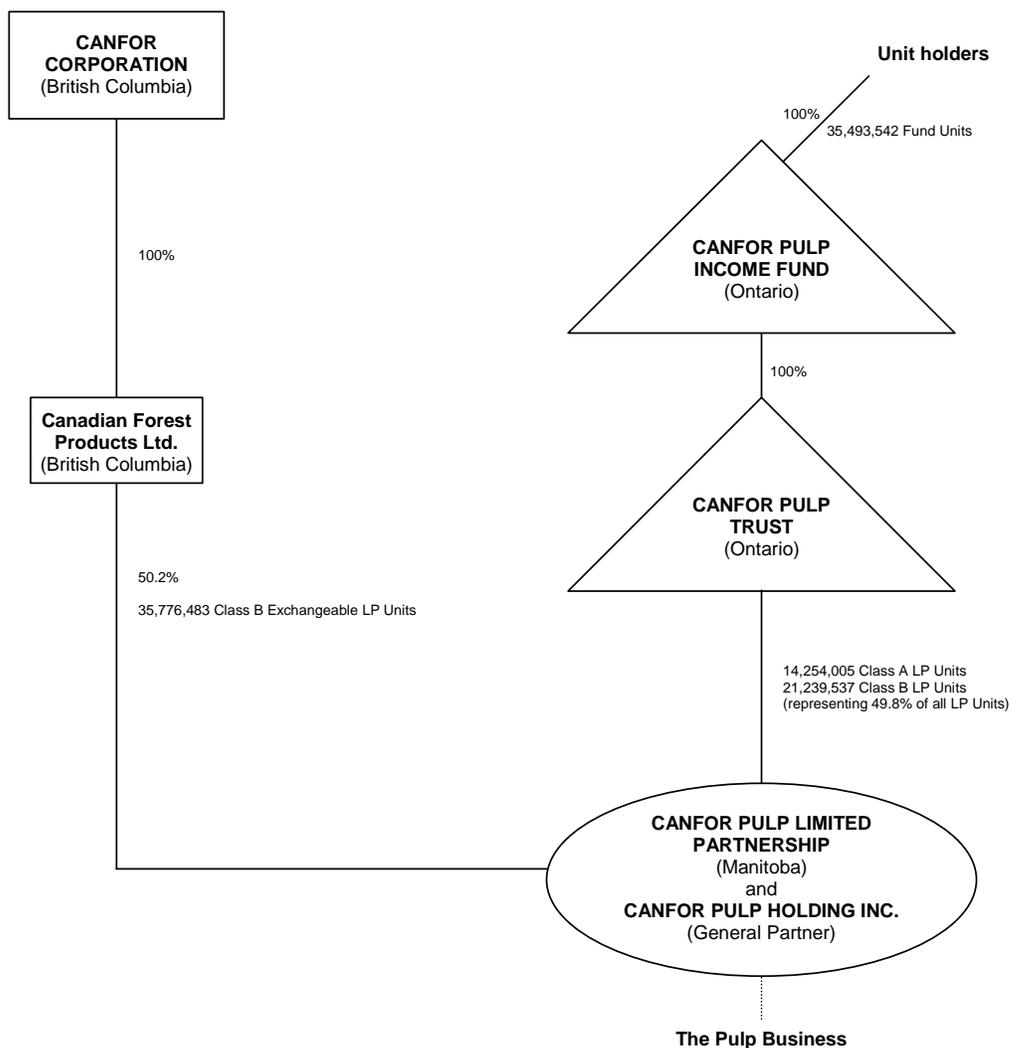
## CANFOR PULP LIMITED PARTNERSHIP

### Structure

The Partnership is a limited partnership formed on April 21, 2006, under the laws of Manitoba to acquire and carry on the NBSK pulp and paper business of Canfor. The business consists of two NBSK pulp mills and one NBSK pulp and paper mill located in Prince George, BC and a marketing group based in Vancouver, BC (the Pulp Business).

At February 19, 2008, the Fund indirectly holds a total of 14,254,005 Class A Limited Partnership Units and 21,239,537 Class B Limited Partnership Units, representing 49.8% of the Partnership and Canfor owns the remaining 50.2%. The Partnership is managed, on behalf of the limited partners, by Canfor Pulp Holding Inc., the General Partner. Below is a simplified schematic of the ownership structure.

### Partnership Structure



## Business

The Partnership is a leading global supplier of pulp and paper products with operations based in the central interior of British Columbia. The Partnership's strategy is to maximize cash flows and enhance the value of its assets by: (i) preserving its low-cost operating position, (ii) maintaining the premium quality of its products and (iii) opportunistically acquiring high quality assets.

The Partnership owns and operates three mills with annual capacity to produce over one million tonnes of northern softwood market kraft pulp, 90% of which is bleached to become NBSK pulp for sale to the market, and approximately 140,000 tonnes of kraft paper.

### SUMMARY OF SELECTED PARTNERSHIP RESULTS

(millions of dollars, except for per unit amounts, unaudited)	<b>Q4 2007</b>	Q3 2007	<b>Year 2007</b>	Q4 2006	Year 2006
Sales <sup>1</sup>	<b>215.1</b>	228.9	<b>921.6</b>	225.2	830.4
EBITDA <sup>1,2</sup>	<b>27.9</b>	48.8	<b>188.5</b>	58.2	180.2
Operating income <sup>1</sup>	<b>11.7</b>	35.4	<b>134.3</b>	45.6	131.2
Net income	<b>12.1</b>	33.2	<b>129.8</b>	44.8	123.0
Per Partnership unit, basic and diluted					
Net income	<b>0.17</b>	0.46	<b>1.82</b>	0.63	1.73
EBITDA <sup>1</sup>	<b>0.39</b>	0.68	<b>2.65</b>	0.82	2.53
Average exchange rate (US\$/Cdn\$) <sup>3</sup>	<b>1.019</b>	0.957	<b>0.930</b>	0.878	0.882

Notes: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

<sup>2</sup> For calculation of EBITDA, see supplementary financial information on pg. 19.

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

EBITDA for the fourth quarter of 2007 decreased by \$20.9 million from the previous quarter and \$30.3 million when compared to the fourth quarter of 2006. The decrease from the prior quarter is mainly attributable to the impact of the stronger Canadian dollar and a 6% increase in manufacturing costs. The Canadian dollar strengthened significantly during the period with the Bank of Canada noon rate averaging 6.5% higher than the previous quarter and peaking at US\$1.09. The negative impact on operating income from the stronger Canadian dollar was approximately \$12 million when compared to the prior quarter. The increase in manufacturing costs was mainly due to higher energy costs as a result of seasonal increases from winter natural gas usage and price, and timing of spending on maintenance. When compared to the prior year quarter the \$30.3 million decrease in EBITDA was primarily due to the impact of the stronger Canadian dollar and higher fibre costs partially offset by increases in NBSK pulp list prices. The impact of the stronger Canadian dollar was approximately \$28 million when compared to the same period last year. Fourth quarter 2007 fibre costs were in line with the previous quarter and 23% higher than the fourth quarter 2006 with the increase mainly attributable to a higher percentage of whole log chipping to mitigate the impact on residual chip supply from continued sawmill downtime in the interior of British Columbia. Offsetting the stronger Canadian dollar and increased manufacturing costs over the prior year period were increased NBSK pulp list prices of approximately 11%.

For the full year 2007, EBITDA improved \$8.3 million when compared to 2006. The impact of the stronger Canadian dollar and substantially higher fibre costs were more than offset by increased NBSK list prices, and higher production and sales volumes for pulp and paper. Pulp realized prices in Canadian dollar terms improved by 9% when compared to the prior year as a 14% improvement in NBSK list price was partially offset by the stronger Canadian dollar. The Bank of Canada noon rate averaged US\$0.930 in 2007 compared to US\$0.882 in 2006 translating into a negative \$39 million impact to EBITDA. Sales volumes for NBSK market pulp and kraft papers increased by 22,100 and 4,900 tonnes respectively when compared to the prior year. Fibre costs increased by 44% when compared to 2006 and were directly related to higher prices for sawmill residual chips and an increase in higher cost whole log chip volume. The increase in sawmill residual chip prices was due to higher pulp mill sales returns and market conditions brought about by reductions in sawmill residual chip volumes. The reduction in sawmill residual chip

volumes precipitated the need to source higher cost whole log chips in 2007. Excluding fibre costs, 2007 unit cash manufacturing costs were maintained at 2006 levels.

## OPERATING RESULTS BY BUSINESS SEGMENT

### Pulp

(millions of dollars unless otherwise noted, unaudited)	<b>Q4 2007</b>	Q3 2007	<b>Year 2007</b>	Q4 2006	Year 2006
Sales <sup>1</sup>	<b>186.0</b>	199.3	<b>798.0</b>	194.3	717.1
EBITDA <sup>1</sup>	<b>31.2</b>	51.9	<b>202.5</b>	59.2	188.8
EBITDA margin <sup>1</sup>	<b>17%</b>	26%	<b>25%</b>	30%	26%
Operating income <sup>1</sup>	<b>16.0</b>	39.5	<b>152.6</b>	47.7	143.8
Average NBSK pulp list price – (US\$ per tonne, delivered to U.S.A.)	<b>857</b>	837	<b>823</b>	770	721
Average NBSK pulp list price (Cdn\$ per tonne, delivered to U.S.A.)	<b>841</b>	875	<b>885</b>	877	817
Production – pulp (000 mt)	<b>261.4</b>	265.7	<b>1,044.3</b>	263.7	1,015.4
Shipments – Partnership-produced pulp (000 mt)	<b>253.6</b>	257.1	<b>1,023.6</b>	249.8	1,001.5
<i>Marketed on behalf of HSLP &amp; Canfor (000 mt)</i>	<b>148.0</b>	139.2	<b>571.9</b>	128.3	570.6

Note: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

Fourth quarter 2007 operating income of the pulp segment decreased by \$23.5 million from the previous quarter and by \$31.7 million when compared to the same quarter in the prior year. When compared to the prior quarter, the negative impact of the stronger Canadian dollar, higher spending on manufacturing costs, lower shipments and one time non-cash adjustments, were only partially offset by improved NBSK list prices. The negative impact on operating income from the stronger Canadian dollar was approximately \$10 million when compared to the prior quarter. The increase in manufacturing costs was mainly due to higher energy costs as a result of seasonal increase from winter natural gas usage and price and timing of spending on maintenance. Fibre costs remained flat quarter over quarter as improvements in whole log chipping operations were realized offsetting an increase in whole log chip deliveries to 21% of total supply from 15% in the prior quarter. The non-cash adjustments were comprised of \$1.0 million to fully amortize the asset retirement obligation related to the Intercon ash pond which was decommissioned in the quarter and a \$1.1 million loss on disposal of non operational capital assets. Shipment volumes of NBSK market pulp decreased slightly from the previous quarter and were consistent with the drop in production.

The fourth quarter 2007 results are lower than those in the same period a year ago, due to the impact of the stronger Canadian dollar, higher fibre costs and one time non-cash adjustments (as above), which were partially offset by increases in NBSK pulp list prices. The impact of the stronger Canadian dollar was approximately \$24 million when compared to the same period last year. Fibre costs increased 23% when compared to the prior year period, mainly attributable to a higher percentage of whole log chipping to mitigate the impact on residual chip supply from continued sawmill downtime in the interior of British Columbia. Offsetting the stronger Canadian dollar and increased fibre costs over the prior year period were increased NBSK pulp list prices of approximately 11%.

When compared to the previous year, 2007 operating income improved by \$8.8 million. The impact of the stronger Canadian dollar and substantially higher fibre costs were more than offset by increased NBSK list prices, and higher production and sales volumes for pulp. Pulp realized prices in Canadian dollar terms improved by 9% when compared to the prior year as a 14% improvement in NBSK list price was partially offset by the stronger Canadian dollar. The impact of the stronger Canadian dollar was approximately \$33 million when compared to the same period last year. Shipments of NBSK market pulp increased by 22,100 tonnes when compared to the prior year. Fibre costs increased by 44% when compared to 2006, directly related to higher prices for sawmill residual chips and an increase in higher cost whole log chip volume.

## *Operations*

NBSK production during the fourth quarter was 4,300 tonnes less than the third quarter and 2,300 tonnes less than the fourth quarter of 2006. Total downtime taken during the quarter was 12 days compared to 10 days in the prior quarter and 2 days in the fourth quarter of 2006. The Prince George Pulp and Paper mill and Northwood mill completed scheduled maintenance outages during the fourth quarter of 2007. Production tonnes lost in the quarter as a result of the downtime was approximately 1,700 tonnes more than the prior quarter. The decrease in production over the prior year quarter was due to there being no scheduled maintenance downtime in the fourth quarter of 2006.

On an annual basis the mills produced a record level of tonnes surpassing the previous record set in 2006 by 31,400 tonnes. The back to back production records for total tonnes in 2006 and 2007 represent an increase of 51,400 tonnes when compared to the prior record set in 2004. Individual mill production records were achieved at the Northwood mill, 589,000 tonnes in 2007 versus 562,000 in 2006 and Prince George Pulp and Paper mill, 280,000 tonnes in 2007 versus the prior record of 279,000 set in 2000. A total of 30 days of scheduled maintenance downtime was taken at the pulp mill facilities, the same number of days as the prior year.

## *Markets*

Market conditions during the fourth quarter of 2007 remained strong. The Pulp and Paper Products Council (PPPC), reported market pulp inventories (World 19 Producers) ended December at 29 days of supply for all grades. Softwood kraft market pulp inventories were at 27 days of supply, one day above where softwood inventories stood at the end of the prior quarter. Generally 30 days of supply of inventory is considered representative of a balanced market. Market pulp shipments for the year were up 3.4% for all grades, but only up 0.9% for softwood pulp. While the shipment levels were healthy, production since the end of the third quarter has outpaced demand, leading to the one-day increase in producer inventories.

The printing and writing paper sector, which is the largest customer sector for the Partnership, has seen flat to slightly lower demand this year versus the same period of 2006. PPPC statistics covering the majority of our markets indicate demand was down 0.6% for the year. However by grade, coated mechanical paper demand, a large consumer of the Partnership's products, was up by 2.5% for the year. Most of the demand reduction was in coated and uncoated woodfree papers, not a target market for the Partnership.

There is still significant supply uncertainty for buyers of northern softwood kraft market pulp. This is primarily due to the impact on Canadian and European producers of the cost and availability of fibre and the weakness of the US dollar. Canadian pulp mills that are reliant on residual woodchips from sawmills are facing supply issues due to the large amount of downtime in the sawmilling sector. In Europe producers also face fibre shortages and competition with biomass energy producers for wood chips.

The announced price for January 2008 for both the USA and Northwest Europe is US\$880 per tonne. This is up US\$30 for the USA and US\$50 for Europe since the beginning of the fourth quarter. By comparison, the fourth quarter of 2006 started and ended with prices at US\$770 per tonne in the USA and US\$730 per tonne in Europe.

## *Outlook – Pulp*

The Partnership's production levels for 2008, with the exception of the reduction related to the previously disclosed fire at the Prince George Pulp and Paper mill, are expected to be similar to 2007. Higher daily operating rates are expected to be offset by slightly longer planned maintenance and capital outages. Both Northwood and Intercontinental mills will extend shutdowns; at Northwood to perform maintenance and modest capital improvements on its digester and recovery boilers and at Intercon to perform similar improvements on its digester and pulp machine. These improvements, which are primarily debottlenecking, will allow production growth to resume in 2009.

The demand and the price for market pulp are expected to remain strong through the first half of 2008. The seasonal decline in demand in the December to February period is typically followed by a surge in demand in the spring. The US election and the summer Olympics in China are expected to bolster demand for pulp throughout much of 2008. Furthermore, the supply of market pulp is curtailed each spring as mills in the northern hemisphere shutdown for annual maintenance. Combined, these market dynamics are expected to keep the pulp market balanced and allow for flat or slightly higher prices over the first half of the year.

## Paper

(millions of dollars unless otherwise noted, unaudited)	Q4 2007	Q3 2007	Year 2007	Q4 2006	Year 2006
Sales <sup>1</sup>	29.1	29.6	123.6	30.9	113.3
EBITDA <sup>1</sup>	0.1	0.6	2.0	2.7	5.5
EBITDA margin <sup>1</sup>	0%	2%	2%	8%	5%
Operating (loss) income <sup>1</sup>	(0.9)	(0.4)	(2.1)	1.7	1.7
Production – paper (000 mt)	33.1	33.0	131.6	33.9	129.1
Shipments – paper (000 mt)	32.4	30.8	129.5	32.7	124.6

Note: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

The operating loss of the paper segment for the fourth quarter of 2007 was \$0.9 million, \$0.5 million more than the prior quarter and a \$2.6 million unfavourable variance when compared to the same quarter last year. The \$0.5 million decrease over the prior quarter was the result of a decrease to realized prices in Canadian dollar terms by 6% and higher spending on manufacturing costs, partially offset by higher shipments and lower raw material costs for slush pulp reflecting the lower Canadian dollar market price for pulp. The decrease in realized prices for paper in Canadian dollar terms was mainly attributable to the stronger Canadian dollar and the increase in manufacturing costs was related to timing of spending on maintenance. When compared to the same period in the prior year the lower operating earnings were due to a 5% decrease in realized prices in Canadian dollar terms and higher spending on maintenance costs as there was no maintenance downtime in the fourth quarter of 2006.

The 2007 operating results were \$3.8 million unfavourable when compared to 2006. The impact of the stronger Canadian dollar and higher costs for slush pulp, which is transferred to the paper mill at market price, were offset by improved paper prices, higher sales volumes and overall improved productivity. Net realized prices in US dollars increased by 11% over the prior year. However, the impacts of the stronger Canadian dollar resulted in only a 5% increase in net realized prices in Canadian terms. Also unfavourably impacting results were the higher costs for slush pulp which increased by 10% over 2006. Partially offsetting this were increased sales volumes of 4,900 tonnes when compared to 2006.

### Operations

Paper production during the fourth quarter improved by 100 tonnes over the prior quarter and was 800 tonnes lower when compared to the same period in 2006. Scheduled maintenance was completed during the quarter representing approximately 1,100 tonnes of lost production as compared to 1,900 tonnes of lost production in the prior quarter. No maintenance downtime was taken during the fourth quarter of 2006. Paper production for the 2007 year improved by 2,500 tonnes when compared to 2006.

### Markets

Global demand for sack kraft paper remained strong through the end of the year with continued upward price movement. Offshore markets showed continued strength in the fourth quarter of 2007. The U.S. market has been impacted by the slowdown in U.S. housing starts with sack paper demand off by 6% during 2007. Offsetting the decrease in sack paper demand was reduced supply of paper imports from Europe as a result of eroding margins due to increased freight rates and the strengthening of the Euro relative to the U.S. dollar.

Note: <sup>1</sup> Paper Shipping Sack Manufacturers' Association statistics

### Outlook – Kraft Paper Markets

Heading into 2008, price increases in the export and to a lesser extent the North American markets are expected. A US\$50 per tonne increase is expected to be fully implemented by the end of the first quarter. Continued supply and demand balance for both white and brown grades leads to a favourable outlook for 2008.

## Non-Segmented Costs

(millions of dollars, unaudited)	Q4 2007	Q3 2007	Year 2007	Q4 2006	Year 2006
Unallocated costs	3.4	3.7	16.2	3.8	14.3
Business acquisition costs	-	-	-	-	5.9
Interest expense, net	1.7	1.6	6.7	2.0	3.8
Unrealized (gain) loss on derivative instruments	(1.8)	3.1	3.3	-	-
Unrealized foreign exchange (gain) loss on long-term debt	(0.9)	(7.4)	(19.5)	2.5	2.5
Foreign exchange (gain) loss on working capital <sup>1</sup>	0.6	4.9	13.8	(3.7)	(3.9)
Other expense (income)	-	-	0.2	-	(0.1)
	3.0	5.9	20.7	4.6	22.5

Note: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

### *Unallocated Costs*

Unallocated costs, comprised principally of general and administrative expenses, totalled \$3.4 million in the fourth quarter of 2007 compared to \$3.7 million in the prior quarter and \$3.8 million in the same period last year. Unallocated costs were down slightly when compared to the prior quarter due to a lower accrual for the 2007 performance based incentive plan payment. When compared to the same period in the prior year the difference mainly relates to lower audit related fees. Total unallocated costs for 2007 of \$16.2 million were \$1.9 million higher than the prior year. The increase over the prior year is mainly attributable to the higher performance based incentive plan expense.

### *Interest Expense*

Net interest expense during the fourth quarter of 2007 was similar to the prior quarter and lower than the prior year primarily due to interest income on higher cash and cash equivalent balances in the quarter. No interest expense is shown for periods prior to July 2006, when the pulp business was an operating segment of Canfor and interest expense was not allocated.

### *Other Non-segmented Items*

The unrealized gains and losses on derivative instruments result from the adoption of the Canadian Institute of Chartered Accountants (CICA) new Handbook Section 3855 "Financial Instruments" at January 1, 2007 and the Partnership's decision to discontinue its policy of hedge accounting. The net unrealized gain of \$1.8 million recorded in the period relates to a revaluation to market of outstanding natural gas swaps at the end of the quarter. The natural gas swaps are used to fix the price on a portion of the Partnership's ongoing natural gas requirements.

The unrealized foreign exchange gain on long-term debt and the foreign exchange loss on working capital are the direct result of translating U.S. dollar balances at period-end exchange rates and reflect the effect of the stronger Canadian dollar.

## SUMMARY OF FINANCIAL POSITION

The following table summarizes the Partnership's financial position as at the end of the following periods:

(millions of dollars, except for ratios, unaudited)	Q4 2007	Year 2007	Q4 2006	Year 2006
Ratio of current assets to current liabilities	1.88	1.88	1.92	1.92
Ratio of net debt to partners' equity <sup>1</sup>	0.18	0.18	0.17	0.17
Increase (decrease) in cash and cash equivalents	(37.9)	(25.8)	11.0	27.8
Comprised of cash flow from (used in):				
Operating activities	5.0	149.7	62.6	168.2
Financing activities	(31.4)	(148.3)	(46.5)	(120.8)
Investing activities	(11.5)	(27.2)	(5.1)	(19.6)

Note: <sup>1</sup> Net debt consists of long-term debt net of cash and cash equivalents.

### Changes in Financial Position

Operating activities generated \$5.0 million in cash in the fourth quarter of 2007 compared to \$62.6 million in the prior year quarter. The decrease was due to lower cash generated as a result of reduced earnings and an increase in cash used in working capital in the fourth quarter of 2007 of \$23.3 million compared to \$1.0 million in the fourth quarter of 2006. The reduced earnings were primarily the result of the stronger Canadian dollar and higher fibre costs when compared to the prior year quarter. The higher use of cash, from increased working capital requirements, was primarily the result of the level and timing of agency sales, and lower chip payables due to sawmill downtime in the fourth quarter of 2007.

For the full year 2007, operating activities generated \$149.7 million in cash compared to \$168.2 million in 2006. The year over year reduction in cash generated is mainly attributable to an increase in working capital in 2007, primarily as a result of higher inventories. The increase in inventories is due to increases in both volume and unit costs of finished pulp and chips. During 2007, the Partnership extended whole log chipping initiatives to mitigate the impact of sawmill curtailments on the supply of sawmill residual chips and to rebuild chip inventories to target levels. The reduced sawmill residual chips depleted chip inventory levels at the end of 2006 and restricted supply throughout 2007. Finished pulp inventories increased in the fourth quarter due to specific customer curtailments. Planned pulp maintenance production curtailments in the first half of 2008 are expected to reduce these inventories to normal levels. Also contributing to the higher finished pulp and chip inventory values at the end of 2007 as compared to 2006, was the higher cost whole log chipping component in ending inventory.

The cash used in financing activities of \$31.4 million in the quarter and \$148.3 million in the year represents distributions paid to the limited partners, Canfor and the Fund. Cash flows from financing activities in the prior year also include net cash transactions with Canfor prior to the spinout on July 1, 2006.

The cash used in investing activities in the quarter is comprised of \$11.5 million relating to capital expenditures net of accruals and non-cash increases in asset retirement obligations.

### LIQUIDITY AND FINANCIAL REQUIREMENTS

At the end of the current quarter, the Partnership had cash and cash equivalents totalling \$2.6 million. Cash and cash equivalents includes cash on hand and highly liquid investments with an original maturity date of 90 days or less. The Partnership does not have holdings in asset backed commercial paper. The Partnership had bank operating lines of credit of \$75.0 million, of which \$27.4 million was reserved for a standby letter of credit issued to BC Hydro.

### OUTSTANDING UNITS

At February 19, 2008, there were 71,270,025 Limited Partnership Units outstanding, of which 35,493,542 units (consisting of 14,254,005 Class A Limited Partnership Units and 21,239,537 Class B Limited Partnership Units) are owned by the Fund through Canfor Pulp Trust and 35,776,483 Class B Exchangeable Limited Partnership Units are owned indirectly by Canfor.

## RELATED PARTY TRANSACTIONS

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2006 audited consolidated financial statements and are based on agreed upon amounts, and are summarized in note 11 of the unaudited interim consolidated financial statements.

## SUBSEQUENT EVENT

On January 15, 2008 a fire at the Partnership's Prince George Pulp and Paper mill caused extensive damage to the chip screening and infeed system. Alternative chip screening and infeed systems are being investigated to minimize pulp production disruptions at this mill. The Partnership has property damage and business interruption insurance to limit the financial loss to the Partnership. The occurrence is not expected to have a material effect on the financial condition of the Partnership.

## RISKS AND UNCERTAINTIES

A comprehensive discussion of risks and uncertainties was included in the Fund's 2006 Annual Report, which is available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com).

## SELECTED QUARTERLY PARTNERSHIP FINANCIAL INFORMATION

(unaudited)	Q4 2007	Q3 2007	Q2 2007	Q1 2007	Q4 2006	Q3 2006	Q2 2006	Q1 2006
<b>Sales and Income</b> (millions of dollars)								
Sales <sup>1</sup>	215.1	228.9	239.4	238.2	225.2	213.6	196.1	195.5
Operating income <sup>1</sup>	11.7	35.4	39.2	48.0	45.6	49.0	16.9	19.7
EBITDA <sup>1</sup>	27.9	48.8	51.7	60.1	58.2	61.8	28.0	32.2
Net income	12.1	33.2	35.9	48.6	44.8	41.9	15.9	20.4
<b>Per Partnership unit</b> (dollars) <sup>2</sup>								
Net income basic and diluted	0.17	0.46	0.51	0.68	0.63	0.59	0.22	0.29
<b>Statistics</b>								
Pulp shipments (000 mt)	253.6	257.1	259.8	253.1	249.8	251.4	244.6	255.7
Paper shipments (000 mt)	32.4	30.8	35.9	30.4	32.7	29.5	31.3	31.1
Average exchange rate (US\$/Cdn\$) <sup>3</sup>								
	1.019	0.957	0.911	0.854	0.878	0.892	0.891	0.866
Average NBSK pulp list price – (US\$ per tonne, delivered to U.S.A.)								
	857	837	810	790	770	757	705	653

Notes: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

<sup>2</sup> Based on Partnership units outstanding at December 31, 2007 (71,270,025) for all periods.

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

Sales are primarily influenced by changes in market pulp prices, sales volumes and fluctuations in Canadian dollar exchange rates. Operating income, net income and EBITDA are primarily impacted by the level of sales and price fluctuations in raw material inputs, energy prices, maintenance costs and the timing of scheduled maintenance downtime. Net income is also impacted by fluctuations in the Canadian dollar, due to the revaluation to the period end rate of U.S. denominated working capital balances and the U.S. denominated long-term debt. The third quarter of 2006 also included a charge for transaction costs of \$5.9 million related to the spinout of Canfor's pulp business into the Partnership.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements. On an ongoing basis, management reviews its estimates, including those related to useful lives for amortization, impairment of long-lived assets, pension and other employee future benefit plans and asset retirement 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 Partnership's financial condition.

## **CHANGES IN ACCOUNTING POLICIES**

### *Employee Future Benefits*

During the first quarter of 2007, the Partnership determined that with respect to its participation in the Canfor salaried pension plans it was able to determine the benefit obligations and the attributable assets related to its employees. The Partnership ceased to account for these pension costs on the basis of a multi-employer plan and has adopted the pronouncements applicable to accounting for defined benefit pension plans. This change is presented on a retroactive basis, without restatement, as the relevant information is not available for prior periods. The Partnership's accounting policy is detailed in notes 3 and 7 of the Partnership's unaudited interim consolidated financial statements.

### *Financial Instruments*

Effective January 1, 2007, the Partnership adopted the Canadian Institute of Chartered Accountants' new Handbook Section 3855 "Financial Instruments – recognition and measurement", Section 3865 "Hedges" and Section 1530 "Comprehensive Income". These standards were adopted retroactively and comparative amounts for prior periods have not been restated.

Section 3855 prescribes when a financial instrument should be recognized on the balance sheet and at what amount. It also specifies how to present financial instrument gains and losses. Under Section 3855, all financial instruments are classified into one of these five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments and derivatives are measured in the Consolidated Balance Sheet at fair value on initial recognition except for certain related party transactions. Subsequent measurement depends on the initial classification of the instrument. Loans and receivables and other financial liabilities are measured at amortized cost. All derivative instruments, including embedded derivatives, are recorded in the Consolidated Balance Sheet at fair value unless they qualify for the normal sales and purchases exemption. Changes in the fair value of derivatives that are not exempt are recorded in income.

As a result of adopting these new standards, the Partnership has classified its cash and cash equivalents as held-for-trading. Accounts receivable are classified as loans and receivables. Bank indebtedness, accounts payable and accrued charges, and long-term debt, including interest payable, are classified as other liabilities, all of which are measured at amortized cost. Derivative instruments are recorded in the balance sheet at fair value, including those derivatives that are embedded in financial or non-financial contracts that are not closely related to the host contract.

As a result of consideration of the new guidance provided in Section 3865 – "Hedges", on a prospective basis, the Partnership has determined not to utilize hedge accounting on its existing derivative instruments. As a result, these instruments, which were previously recorded using hedge accounting, were measured at fair value on January 1, 2007 with a corresponding adjustment through accumulated other comprehensive income (see note 16 of the Partnership's unaudited interim consolidated financial statements).

Section 1530 introduces new requirements for situations when certain gains and losses ("other comprehensive income") must be temporarily presented outside of net income in a new Statement of Comprehensive Income. Comprehensive income is the change in the Partnership's equity that results from transactions, events and circumstances from sources other than the Partners. For the quarter ended March 31, 2007, the Partnership recorded the reversal of unrealized losses on derivative instruments outstanding at December 31, 2006 in other comprehensive income. These derivative instruments had previously been accounted for as cash flow hedges and recorded in accordance with hedge accounting.

In accordance with the transitional provisions, the Partnership has transferred the balance of deferred financing costs relating to the credit facilities and long-term debt entered into on November 30, 2006 to Opening Partners' Equity at January 1, 2007.

### *Asset Retirement Obligations*

The Partnership maintains several ash ponds and landfills to dispose of fly ash from the power boilers. During the quarter ended September 30, 2007, the Partnership recognized asset retirement obligations in respect of landfill closure and post-closure monitoring costs. The change reflected new information on all sites concerning the estimated timing of closure and closure alternatives. As a result, the Partnership recorded an obligation based on the fair value of the landfill closure costs of \$9.1 million with a corresponding capital addition to the related assets. This estimate is based on expected closure of the respective mill landfills occurring in periods ranging from 10 to 25 years.

During the second quarter of 2007 an environmental containment liability was identified at the Intercon mill site arising from the normal operation of the ash pond. As a result, the Partnership recorded an obligation based on the fair value of the containment estimate of \$2.4 million, with a corresponding capital addition to the related asset. The ash pond was decommissioned and remediation work commenced in the fourth quarter.

The Partnership has certain assets that have indeterminate useful lives and, therefore, there is an indeterminate settlement date for the related asset retirement obligation. As a result, no asset retirement obligations are recorded for these assets. These assets include, for example, wastewater and effluent ponds that will have to be drained once the related operating facility is closed and storage sites for which removal of chemicals and other related materials will be required once the related operating facility is closed. Once the useful life of these assets becomes determinable and an estimate of fair value can be made, an asset retirement obligation will be recorded.

### **NEW ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED**

The CICA has issued three new standards that may affect the financial disclosures and results of operations of the Partnership for interim and annual periods beginning January 1, 2008. The Partnership will adopt the requirements commencing in the interim period ended March 31, 2008 and is considering the impact this will have on the Partnership's financial statements.

#### *Section 1535 – Capital Disclosures*

This Section establishes standards for disclosing information about an entity's capital and how it is managed. Under this standard the Partnership will be required to disclose the following, based on the information provided internally to the entity's key management personnel:

- (i) qualitative information about its objectives, policies and processes for managing capital;
- (ii) summary quantitative data about what it manages as capital;
- (iii) whether during the period it complied with any externally imposed capital requirements to which it is subject;
- (iv) when the Partnership has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

#### *Section 3031 - Inventories*

This Section prescribes the accounting treatment for inventories and provides guidance on the determination of costs and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

#### *Section 3862 – Financial Instruments – Disclosures*

This Section requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks. Entities will be required to disclose the measurement basis or bases used, and the criteria used to determine classification for different types of instruments.

The Section requires specific disclosures to be made, including the criteria for:

- (i) designating financial assets and liabilities as held for trading;
- (ii) designating financial assets as available-for-sale; and
- (iii) determining when impairment is recorded against the related financial asset or when an allowance account is used.

**CANFOR PULP LIMITED PARTNERSHIP**  
**SUPPLEMENTARY FINANCIAL INFORMATION**

	3 months ended		Year ended	
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
(millions of dollars, unaudited)				
<b>RECONCILIATION OF NET INCOME TO EBITDA</b>				
<b>Net Income</b>	\$ 12.1	\$ 44.8	\$ 129.8	\$ 123.0
Add (deduct):				
Amortization	14.8	12.6	52.8	49.0
Net interest expense	1.7	2.0	6.7	3.8
Unrealized foreign exchange loss (gain) on long-term debt	(0.9)	2.5	(19.5)	2.5
Unrealized loss (gain) on derivative instruments	(1.8)	-	3.3	-
Foreign exchange loss (gain) on working capital	0.6	(3.7)	13.8	(3.9)
Loss on disposal of fixed assets	1.1	-	1.1	-
Other expense	0.3	-	0.5	(0.1)
Business acquisition costs	-	-	-	5.9
<b>EBITDA</b>	\$ 27.9	\$ 58.2	\$ 188.5	\$ 180.2

	3 months ended		Year ended	Six months Ended <sup>1</sup>
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
(millions of dollars, unaudited)				
<b>CALCULATION OF STANDARDIZED AND ADJUSTED DISTRIBUTABLE CASH</b>				
<b>Cash flow from operating activities</b>	\$ 5.0	\$ 62.6	\$ 149.7	\$ 99.9
Deduct: Capital expenditures – cash	(11.5)	(5.1)	(23.8)	(11.1)
<b>Standardized distributable cash</b>	\$ (6.5)	\$ 57.5	\$ 125.9	\$ 88.8
<b>Adjustments to standardized distributable cash:</b>				
Add (deduct):				
Increase in non-cash working capital	23.3	1.0	25.0	22.8
Capital expenditures – accruals	(3.2)	-	(8.1)	-
Financing Costs	-	(1.6)	-	(1.6)
Salary pension plan contribution <sup>2</sup>	-	-	(3.4)	-
<b>Adjusted distributable cash</b>	\$ 13.6	\$ 56.9	\$ 139.4	\$ 110.0
Standardized distributable cash – per Partnership unit (in dollars)	\$ (0.09)	\$ 0.81	\$ 1.77	\$ 1.25
Adjusted distributable cash – per Partnership unit (in dollars)	\$ 0.19	\$ 0.80	\$ 1.96	\$ 1.54
<b>Cash distributions declared (paid and payable)</b>	27.1	57.1	131.1	88.5
Cash distributions declared – per Partnership unit (in dollars)	\$ 0.38	\$ 0.80	\$ 1.84	\$ 1.24

Notes: <sup>1</sup>For the purposes of presenting Standardized Distributable cash, Adjusted Distributable cash and Cash Distributions, the 2006 comparative figures are for the six months ended December 31, 2006, as the Partnership did not exist prior to July 1, 2006, and as a result there were no cash distributions made prior to July 1, 2006.

<sup>2</sup>\$3.4 million pension contribution representing a payment above the normal funding requirements which was used to reduce the 2006 taxable income of the Partnership.

**STANDARDIZED DISTRIBUTABLE CASH AND CASH DISTRIBUTIONS**

In accordance with the Canadian Institute of Chartered Accountants July 2007 interpretive release “Standardized Distributable Cash in Income Trusts and other Flow-Through Entities”, the Partnership has adopted the distributable cash calculation which conforms with the current guidance. In summary, for the purposes of the Partnership, standardized distributable cash is defined as the periodic cash flows from operating activities as reported in the GAAP financial statements, including the effects of changes in non-cash working capital less total capital expenditures as reported in the GAAP financial statements.

Management determines the level of cash distributions based on the level of cash flow from operations before working capital changes less actual and planned capital expenditures, a reserve for future major capital replacements (estimated at \$4 million per year) and a contingency reserve. During the year distributions are based on estimates of full year cash flow and capital spending; thus distributions may be adjusted as these estimates change. It is expected that normal seasonal fluctuations in working capital will be funded from cash resources or the revolving short-term credit facility, and thus will not significantly affect the level of distributions.

Distributions are declared monthly with date of record on the last day of the month and payable within 15 days following. The Partnership began active operation, including monthly distributions, in July 2006 and thus there were no distributions prior to that date.

**Canfor Pulp Income Fund**  
**Consolidated Statements of Income, Comprehensive Income and Accumulated Earnings and Distributions**

(thousands of dollars, except unit and per unit amounts, unaudited)	3 months ended		Year ended
	December 31, 2007	December 31, 2006	December 31, 2007
<b>Income</b>			
Equity income in Canfor Pulp Limited Partnership	\$ 5,999	\$ 12,184	\$ 64,643
<b>Net income before future income taxes</b>	<b>5,999</b>	12,184	<b>64,643</b>
Future income taxes (recovery) (note 7)	(2,704)	-	36,633
Net income	8,703	12,184	28,010
Distributions declared (note 4)	(13,487)	(24,147)	(65,308)
Earnings in excess of distributions - surplus (deficit)	(4,784)	(11,963)	(37,298)
<b>Weighted average number of units</b>	<b>35,493,542</b>	21,641,670	<b>35,493,542</b>
<b>Net income per Fund unit, basic and diluted (in dollars)</b>	<b>\$ 0.25</b>	\$ 0.56	<b>\$ 0.79</b>
Net income for the period	\$ 8,703	\$ 12,184	\$ 28,010
Other comprehensive income			
Equity interest in other comprehensive income (loss) of Canfor Pulp Limited Partnership	(20)	-	1,185
<b>Comprehensive income</b>	<b>\$ 8,683</b>	\$ 12,184	\$ 29,195
<b>Accumulated Earnings and Distributions</b>			
Balance, beginning of period – Accumulated earnings in excess of distributions - surplus (deficit)	\$ (40,012)	\$ 2,102	\$ (9,861)
Accounting policy change (note 2)	-	-	2,363
Balance, beginning of period – Accumulated earnings in excess of distributions - surplus (deficit), as restated	(40,012)	2,102	(7,498)
Earnings in excess of distributions - surplus (deficit) - current period	(4,784)	(11,963)	(37,298)
<b>Balance, end of period – Accumulated earnings in excess of distributions - surplus (deficit)</b>	<b>\$ (44,796)</b>	\$ (9,861)	<b>\$ (44,796)</b>

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

**Canfor Pulp Income Fund**  
**Consolidated Statements of Cash Flows**

(thousands of dollars, unaudited)	3 months ended		Year ended
	December 31, 2007	December 31, 2006	December 31, 2007
<b>Cash generated from (used in)</b>			
<b>Operating activities</b>			
Net income	\$ 8,703	\$ 12,184	\$ 28,010
Distributions received from Canfor Pulp Limited Partnership	15,617	14,220	73,827
Items not affecting cash:			
Equity income in Canfor Pulp Limited Partnership	(5,999)	(12,184)	(64,643)
Future income taxes (note 7)	(2,704)	-	36,633
	15,617	14,220	73,827
<b>Financing activities</b>			
Distributions paid to Unitholders	\$ (15,617)	\$ (14,220)	\$ (73,827)
<b>Beginning, change and ending balance in cash and cash equivalents</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>

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

**Canfor Pulp Income Fund  
Consolidated Balance Sheets**

(thousands of dollars, unaudited)	As at December 31, 2007	As at December 31, 2006
<b>ASSETS</b>		
<b>Current Assets</b>		
Distributions receivable from Canfor Pulp Limited Partnership (note 5)	\$ 4,259	\$ 12,778
Total current assets	4,259	12,778
<b>Equity investment in Canfor Pulp Limited Partnership (note 3)</b>	<b>291,458</b>	289,490
	<b>\$ 295,717</b>	<b>\$ 302,268</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Distribution payable (note 4)	4,259	12,778
Total current liabilities	4,259	12,778
<b>Future income taxes (note 7)</b>	<b>36,633</b>	-
	<b>40,892</b>	12,778
<b>UNITHOLDERS' EQUITY</b>		
Unitholders' equity - 35,493,542 Fund units outstanding	299,351	299,351
Accumulated earnings and distributions	(44,796)	(9,861)
Accumulated other comprehensive income (note 6)	270	-
Total Unitholders' Equity	254,825	289,490
	<b>\$ 295,717</b>	<b>\$ 302,268</b>

Description of the fund and basis of presentation of financial statements (note 1).

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

Approved by the Trustees

Stan Bracken-Horrocks

Charles Jago

## **Canfor Pulp Income Fund**

### **Notes to the Unaudited Interim Consolidated Financial Statements as at December 31, 2007**

#### **1. Description of the Fund and Basis of Presentation of Financial Statements**

Canfor Pulp Income Fund (the Fund) is an unincorporated open-ended trust established under the laws of Ontario on April 21, 2006, pursuant to the Fund Declaration. The principal head office of the Fund is located at 1700 West 75<sup>th</sup> Avenue, Vancouver, B.C., Canada. The Fund has been established to acquire and hold, through a wholly owned trust, the Canfor Pulp Trust (the Trust), investments in the Limited Partnership Units of the Canfor Pulp Limited Partnership (the Partnership), and such other investments as the Trustees of the Fund may determine. The general partner of the Partnership is Canfor Pulp Holding Inc. (the General Partner) and each partner holds an ownership interest in the General Partner equal to its Partnership interest.

These unaudited interim consolidated financial statements include the accounts of the Fund and the Trust. From the date of its establishment on April 21, 2006 to June 30, 2006 the Fund was inactive. As a result there are no comparative figures in the unaudited interim consolidated financial statements for the 12 months ended December 31, 2006.

Each unitholder participates pro-rata in any distributions from the Fund.

The Fund is entirely dependent on distributions from the Partnership to make its own distributions.

#### **2. Significant Accounting Policies, Changes and New Pronouncements Not Yet Adopted**

These unaudited interim consolidated financial statements do not include all of the disclosures required by Canadian generally accepted accounting principles for annual financial statements and, accordingly, should be read in conjunction with the audited consolidated financial statements and notes included in the Fund's 2006 Annual Report. These unaudited interim consolidated financial statements follow the same accounting policies and methods of computation as used in the 2006 audited consolidated financial statements, except as noted below.

##### *Financial Instruments*

Effective January 1, 2007, the Partnership adopted the Canadian Institute of Chartered Accountants' new Handbook Section 3855 "Financial Instruments – recognition and measurement" and Section 1530 "Comprehensive Income". These standards were adopted retroactively and comparative amounts of prior periods have not been restated.

Section 3855 prescribes when a financial instrument should be recognized on the balance sheet and at what amount. It also specifies how to present financial instrument gains and losses. Under Section 3855, all financial instruments are classified into one of these five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments and derivatives are measured in the Consolidated Balance Sheets at fair value on initial recognition except for certain related party transactions. Subsequent measurement depends on the initial classification of the instrument. Loans and receivables, held-to-maturity investments and other financial liabilities are measured at amortized cost. All derivative instruments, including embedded derivatives, are recorded in the Consolidated Balance Sheets at fair value unless they qualify for the normal sales and purchases exemption. Changes in the fair value of derivatives that are not exempt are recorded in income.

As a result of adopting these new standards, the Fund has classified its distribution receivable as loans and receivables. Distributions payable are classified as other liabilities and are measured at amortized cost.

Section 1530 introduces new requirements for situations when certain gains and losses ("other comprehensive income") must be temporarily presented outside of net income in a new Statement of Comprehensive Income. Comprehensive income is the change in the Fund's Unitholder's equity that result from transactions, events and circumstances from sources other than the Unitholders. For the period ended December 31, 2007, the Fund's other comprehensive income resulted from its equity interest in the Partnership (see notes to the Partnership's unaudited interim consolidated financial statements).

### *Future Income Taxes*

In June 2007 legislation was substantively enacted to tax distributions of publicly traded income trusts, commencing in 2011. As a result, the Fund is now required to recognize the future income tax assets and liabilities expected to arise when the tax on distributions becomes applicable.

Future income tax assets and liabilities are determined based on the difference between the tax basis of the Fund's and Partnership's assets and liabilities and the respective amounts reported in the financial statements. Future tax assets or liabilities are calculated using the substantively enacted tax rates for the periods in which the differences are expected to be settled. Future tax assets are recognized to the extent that they are considered more likely than not to be realized.

### *New Accounting Pronouncements Not Yet Adopted*

The CICA has issued two new standards which may affect the financial disclosures and results of operations of the Fund for interim and annual periods beginning January 1, 2008. The Fund will adopt the requirements commencing in the interim period ended March 31, 2008 and is considering the impact this will have on the Fund's financial statements.

#### 1. Section 1535 – Capital Disclosures

This Section establishes standards for disclosing information about an entity's capital and how it is managed. Under this standard the Fund will be required to disclose the following, based on the information provided internally to the entity's key management personnel:

- (i) qualitative information about its objectives, policies and processes for managing capital;
- (ii) summary quantitative data about what it manages as capital;
- (iii) whether during the period it complied with any externally imposed capital requirements to which it is subject;
- (iv) when the Fund has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

#### 2. Section 3862 – Financial Instruments – Disclosures

This Section requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks. Entities will be required to disclose the measurement basis or bases used, and the criteria used to determine classification for different types of instruments.

The Section requires specific disclosures to be made, including the criteria for:

- (i) designating financial assets and liabilities as held for trading;
- (ii) designating financial assets as available-for-sale; and
- (iii) determining when impairment is recorded against the related financial asset or when an allowance account is used.

### 3. Equity Investment in Canfor Pulp Limited Partnership

The Fund's equity investment in the Partnership is as follows:

(thousands of dollars, unaudited)	Year ended December 31, 2007	6 months ended December 31, 2006
Balance, beginning of period	289,490	116,560
Accounting policy change – Partners' equity of the Partnership	2,363	-
Accounting policy change – Accumulated other comprehensive income of the Partnership (note 6)	(915)	-
Issuance of Fund units for exchangeable Partnership units (November 30, 2006) – 21,239,537 Fund units	-	182,791
Equity in income of the Partnership	64,643	20,558
Equity interest in other comprehensive income of the Partnership	1,185	-
Distributions earned	(65,308)	(30,419)
Balance, end of period	291,458	289,490

Accounting policy changes above represent the Fund's share (49.8%) of the Partnership's adjustments to opening Partners' equity arising from the adoption of new accounting pronouncements and changes in accounting policies, all as described in notes to the unaudited interim consolidated financial statements of the Partnership.

### 4. Distributions

The Fund declared distributions during the 12 months of 2007 as follows:

(thousands of dollars, except per unit amounts, unaudited)			
Record Date	Payable Date	Amount per Fund Unit \$	Amount \$
January 31, 2007	February 15, 2007	0.14	4,969
February 28, 2007	March 15, 2007	0.14	4,969
March 30, 2007	April 13, 2007	0.14	4,969
April 30, 2007	May 15, 2007	0.14	4,969
May 31, 2007	June 15, 2007	0.18	6,389
June 29, 2007	July 13, 2007	0.18	6,389
July 31, 2007	August 15, 2007	0.18	6,389
August 31, 2007	September 14, 2007	0.18	6,389
September 28, 2007	October 15, 2007	0.18	6,389
October 31, 2007	November 15, 2007	0.14	4,969
November 30, 2007	December 14, 2007	0.12	4,259
December 31, 2007	January 15, 2008	0.12	4,259
		1.84	65,308

The Fund's monthly distributions are based on the Partnership's monthly distributions.

Monthly cash distributions from the Partnership are based on the Partnership's cash flow and are not directly equal to the Fund's pro-rata share of the Partnership's income under the equity method.

### 5. Related Party Transactions

All accounting, treasury, legal and administrative functions for the Fund are performed on its behalf by the Partnership pursuant to a support agreement. Distributions earned from the Partnership for the 3 months and year ended December 31, 2007 were \$13.5 million and \$65.3 million respectively of which \$9.2 million and \$61.0 million were paid, with the balance of \$4.3 million receivable on December 31, 2007.

## 6. Accumulated Other Comprehensive Income

(thousands of dollars, unaudited)	Year ended December 31, 2007
Balance, beginning of period – January 1, 2007	-
Accounting policy change - Accumulated other comprehensive loss of the Partnership	(915)
Balance, beginning of period – January 1, 2007 as restated	(915)
Other comprehensive income	1,185
Balance, end of period	270

## 7. Future Income Taxes

The following table reconciles the income tax expense calculated using statutory tax rates to the actual income tax expense.

(thousands of dollars, unaudited)	Year ended December 31, 2007	6 months ended December 31, 2006
Expected income tax expense at statutory tax rate of nil (2006 – nil)	-	-
Future income taxes on temporary differences	36,633	-
	36,633	-

The temporary differences based on the Fund's 49.8% ownership of the Partnership are as follows:

(thousands of dollars, unaudited)	December 31, 2007
Future income tax liability:	
Equity investment in the Partnership	46,747
Expected reversal of temporary differences prior to 2011	(10,114)
	36,633

Based on a current estimate of the income tax liability at the beginning of 2011, the Fund has recorded a future income tax liability and corresponding non-cash future tax charge to net income. This non-cash charge relates to the Fund's 49.8% ownership in the Partnership and is based on temporary differences between the accounting and tax basis of the Partnership's assets and liabilities expected to reverse after January 1, 2011.

## 8. Financial Instruments

The Fund's financial instruments consist of distributions receivable from the Partnership and distributions payable to unitholders. The fair values of these financial instruments approximate their carrying values due to the relatively short period to maturity of these instruments.

## 9. Segmented Information

The Fund operates in one industry segment, namely investing in pulp and paper producing assets in one geographic region, Canada.

## Canfor Pulp Limited Partnership

### Consolidated Statements of Income, Comprehensive Income and Partners' Equity

(millions of dollars, unaudited)	3 months ended December 31,		Year ended December 31,	
	2007	2006	2007	2006 (note 1)
<b>Sales</b>	\$ 215.1	\$ 225.2	\$ 921.6	\$ 830.4
<b>Costs and expenses</b>				
Manufacturing and product costs	155.5	132.5	597.7	512.7
Freight and other distribution costs	26.3	28.3	111.0	114.1
Amortization	14.8	12.6	52.8	49.0
Selling and administration costs	6.8	6.2	25.8	23.4
	<b>203.4</b>	179.6	<b>787.3</b>	699.2
<b>Operating income</b>	<b>11.7</b>	45.6	<b>134.3</b>	131.2
Interest expense, net	(1.7)	(2.0)	(6.7)	(3.8)
Unrealized foreign exchange gain (loss) on long-term debt	0.9	(2.5)	19.5	(2.5)
Unrealized gain (loss) on derivative instruments (note 13)	1.8	-	(3.3)	-
Foreign exchange gain (loss) on working capital	(0.6)	3.7	(13.8)	3.9
Business acquisition costs	-	-	-	(5.9)
Other income (expense)	-	-	(0.2)	0.1
	<b>0.4</b>	(0.8)	<b>(4.5)</b>	(8.2)
<b>Net Income</b>	<b>12.1</b>	44.8	<b>129.8</b>	123.0
Other comprehensive income (loss)				
Adjustment for realized derivatives (note 16)	(0.1)	-	2.3	-
<b>Comprehensive Income</b>	<b>\$ 12.0</b>	\$ 44.8	<b>\$ 132.1</b>	\$ 123.0
<b>Net income per Partnership unit</b> (in dollars) (note 12)				
Basic and diluted	\$ 0.17	\$ 0.63	\$ 1.82	\$ 1.73
<b>Weighted average Partnership units outstanding</b>	<b>71,270,025</b>	71,270,025	<b>71,270,025</b>	71,270,025
<b>Partners' Equity</b>				
Balance, beginning of period	\$ 600.0	\$ 593.3	\$ 581.0	\$ 728.7
Accounting policy change (note 3)	-	-	2.9	-
Balance, beginning of period as restated	<b>600.0</b>	593.3	<b>583.9</b>	728.7
Net transactions with Canfor	-	-	-	(57.2)
Issuance of promissory note on acquisition	-	-	-	(125.0)
Net Income	12.1	44.8	129.8	123.0
Distributions to partners (note 15)	(27.1)	(57.1)	(131.1)	(88.5)
Other comprehensive income (loss) (note 16)	(0.1)	-	2.3	-
<b>Balance, end of period</b>	<b>\$ 584.9</b>	\$ 581.0	<b>\$ 584.9</b>	\$ 581.0

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

**Canfor Pulp Limited Partnership**  
**Consolidated Statements of Cash Flows**

	3 months ended December 31		Year ended December 31	
	2007	2006	2007	2006
(millions of dollars, unaudited)				(note 1)
<b>Cash and cash equivalents generated from (used in)</b>				
<b>Operating activities</b>				
Net income	\$ 12.1	\$ 44.8	\$ 129.8	\$ 123.0
Items not affecting cash:				
Amortization	14.8	12.6	52.8	49.0
Unrealized foreign exchange loss (gain) on long-term debt	(0.9)	2.5	(19.5)	2.5
Unrealized loss (gain) on derivative instruments	(1.8)	-	3.3	-
Employee future benefits	1.5	1.5	5.2	7.5
Loss on disposal of fixed assets	1.1	-	1.1	-
Other	1.5	2.2	2.0	(3.3)
Cash flow from operations before working capital changes	28.3	63.6	174.7	178.7
Increase in non-cash working capital (note 14)	(23.3)	(1.0)	(25.0)	(10.5)
Cash flow from operating activities	5.0	62.6	149.7	168.2
<b>Financing activities</b>				
Payment of promissory note	-	(125.0)	-	(125.0)
Proceeds of long-term debt	-	125.7	-	125.7
Financing costs	-	(1.6)	-	(1.6)
Distributions paid to partners	(31.4)	(45.6)	(148.3)	(62.7)
Net transactions with Canfor	-	-	-	(57.2)
	(31.4)	(46.5)	(148.3)	(120.8)
<b>Investing activities</b>				
Property, plant and equipment, net (note 14)	(11.5)	(5.1)	(23.8)	(19.6)
Salary pension plan contribution	-	-	(3.4)	-
	(11.5)	(5.1)	(27.2)	(19.6)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>(37.9)</b>	11.0	<b>(25.8)</b>	27.8
<b>Cash and cash equivalents, beginning of period</b>	<b>40.5</b>	17.4	<b>28.4</b>	0.6
<b>Cash and cash equivalents, end of period</b>	<b>\$ 2.6</b>	\$ 28.4	<b>\$ 2.6</b>	\$ 28.4

Supplementary cash flow information (note 14).

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

**Canfor Pulp Limited Partnership  
Consolidated Balance Sheets**

(millions of dollars, unaudited)	As at December 31, 2007	As at December 31, 2006
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 2.6	\$ 28.4
Accounts receivable (note 11)		
Trade	145.6	130.9
Other	9.9	6.7
Inventories (note 4)	136.8	111.0
Prepaid expenses	15.6	13.1
<b>Total current assets</b>	<b>310.5</b>	290.1
<b>Property, plant and equipment</b> (note 5)	<b>585.6</b>	598.6
<b>Deferred charges and other assets</b> (note 6)	<b>12.9</b>	5.0
	<b>\$ 909.0</b>	<b>\$ 893.7</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 11)	\$ 156.9	\$ 125.5
Distributions payable (note 15)	8.6	25.8
<b>Total current liabilities</b>	<b>165.5</b>	151.3
<b>Long-term debt</b> (note 9)	<b>108.7</b>	128.2
<b>Long-term liabilities</b> (note 10)	<b>49.9</b>	33.2
	<b>\$ 324.1</b>	<b>\$ 312.7</b>
<b>PARTNERS' EQUITY</b> – 14,254,005 Class A Limited Partnership Units and 57,016,020 Class B Limited Partnership Units (note 1)	<b>584.9</b>	581.0
	<b>\$ 909.0</b>	<b>\$ 893.7</b>

Subsequent event (note 18)

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

Approved on behalf of Canfor Pulp Limited Partnership by its  
General Partner, Canfor Pulp Holding Inc.,

Stan Bracken-Horrocks  
Director

Paul Richards  
Director

## **Canfor Pulp Limited Partnership**

### **Notes to the Unaudited Interim Consolidated Financial Statements as at December 31, 2007**

#### **1. Business Description and Basis of Presentation**

Canfor Pulp Limited Partnership (the Partnership) is a limited partnership formed on April 21, 2006, under the laws of Manitoba, to acquire and carry on the NBSK pulp and paper business of Canadian Forest Products Ltd. a subsidiary of Canfor Corporation (collectively Canfor). The business consists of two NBSK pulp mills and one NBSK pulp and paper mill located in Prince George, British Columbia and a marketing group based in Vancouver, British Columbia (the Pulp Business).

At December 31, 2007, Canfor owns 50.2% and Canfor Pulp Income Fund (the Fund) indirectly owns 49.8% of the issued and outstanding units of the Partnership.

The general partner of the Partnership is Canfor Pulp Holding Inc. (the General Partner), which holds an interest of 0.001% of the Partnership.

For all periods ending prior to July 1, 2006, these unaudited interim consolidated financial statements present the financial position, results of operations, and cash flows of the Pulp Business on a carve out basis from Canfor as if operated as a stand-alone partnership entity subject to Canfor control. As a result, the transaction has been accounted for as a continuity of interests. For these periods, the accompanying financial statements include allocations of certain of Canfor's assets, liabilities and costs. The financial condition, results of operations, and cash flows of the Pulp Business for these comparative periods are not necessarily indicative of the financial condition, results of operations or cash flows that would have been incurred if the Pulp Business were a separate legal entity. Prior to July 1, 2006, the Pulp Business did not operate bank accounts independent or separate from Canfor (other than for marketing subsidiaries) and, as a result and for purposes of prior periods, the combined effect of all transactions is reflected in "Net transactions with Canfor" in Partners' equity.

These unaudited interim consolidated financial statements are those of the Partnership and do not include the assets, liabilities, revenues and expenses of its partners. The Partnership, other than its incorporated subsidiaries, is not subject to income taxes as its income is allocated for tax purposes to its partners. Accordingly, no recognition has been made for income taxes related to Partnership income in these financial statements. The tax attributes of the Partnership's net assets flow directly to the partners.

Certain comparative figures have been reclassified to conform to current year presentation.

#### *Economic Dependence*

The Partnership depends on Canfor to provide approximately 66% (2006 – 64%) of its fibre supply as well as to provide certain key business and administrative services as described in the Fund's 2006 Annual Report. As a result of these relationships the Partnership considers its operations to be dependent on its ongoing relationship with Canfor.

#### **2. Significant Accounting Policies**

These unaudited interim consolidated financial statements do not include all of the note disclosures required by Canadian generally accepted accounting principles for annual financial statements. Except as described in note 3, the Partnership's accounting policies are as disclosed in the annual audited consolidated financial statements included in the Fund's 2006 Annual Report available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com).

### 3. Changes in Accounting Policies and New Pronouncements Not Yet Adopted

The accounting policy changes impacting Partners' equity at January 1, 2007 are comprised of the following:

(millions of dollars, unaudited)

Defined benefit pension plans	6.3
Deferred financing costs	(1.6)
Accumulated other comprehensive income (note 16)	(1.8)
	2.9

The aggregate adjustment resulting from the change in accounting policy and the adoption of new accounting pronouncements was an increase of \$2.9 million to opening Partners' equity.

#### *Employee Future Benefits*

During the first quarter of 2007, the Partnership determined that with respect to its participation in the Canfor salaried pension plans it was able to determine the benefit obligations and the attributable assets related to its employees. The Partnership ceased to account for these pension costs on the basis of a multi-employer plan and adopted the pronouncements applicable to accounting for defined benefit pension plans. This change is presented on a retroactive basis, without restatement, as the relevant information is not available for prior periods. The Partnership's policy is included below and details are provided in note 7.

The Partnership accrues the costs and related obligations of the defined benefit pension plan using the projected benefit actuarial method prorated on service and management's best estimates of salary escalation and other relevant factors. Actuarial gains and losses arise from changes in actuarial assumptions used to determine the accrued benefit obligation. The excess of the net accumulated actuarial gain or loss over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the average remaining service period of the active employees, which is 10 years. Past service costs arising from plan amendments are deferred and amortized on a straight-line basis over the average remaining service period of employees active at the date of the amendment. On January 1, 2000, the Pulp Business (Canfor) adopted the new recommendations of the Canadian Institute of Chartered Accountants relating to the accounting for pensions and other post employment benefits using the prospective application method. The Partnership is amortizing the transitional obligation on a straight-line basis over 16 years, which was the average remaining service period of employees expected to receive benefits under the benefit plan as of January 1, 2000.

#### *Financial Instruments*

Effective January 1, 2007, the Partnership adopted the Canadian Institute of Chartered Accountants' new Handbook Section 3855 "Financial Instruments – recognition and measurement", Section 3865 "Hedges" and Section 1530 "Comprehensive Income". These standards were adopted retroactively and comparative amounts of prior periods have not been restated.

Section 3855 prescribes when a financial instrument should be recognized on the balance sheet and at what amount. It also specifies how to present financial instrument gains and losses. Under Section 3855, all financial instruments are classified into one of these five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments and derivatives are measured in the Consolidated Balance Sheet at fair value on initial recognition except for certain related party transactions. Subsequent measurement depends on the initial classification of the instrument. Loans and receivables and other financial liabilities are measured at amortized cost. All derivative instruments, including embedded derivatives, are recorded in the Consolidated Balance Sheet at fair value unless they qualify for the normal sales and purchases exemption. Changes in the fair value of derivatives that are not exempt are recorded in income.

As a result of adopting these new standards, the Partnership has classified its accounts receivable as loans and receivables. Bank indebtedness, accounts payable and accrued liabilities, and long-term debt, including interest payable, are classified as other liabilities, all of which are measured at amortized cost. Derivative instruments are

recorded in the balance sheet at fair value, including those derivatives that are embedded in financial or non-financial contracts that are not closely related to the host contract.

As a result of consideration of the new guidance provided in Section 3865 – “Hedges”, on a prospective basis, the Partnership has determined not to utilize hedge accounting on its existing derivative instruments. As a result, these instruments, which were previously recorded using hedge accounting, were measured at fair value on January 1, 2007 with a corresponding adjustment through accumulated other comprehensive income (see note 16).

Section 1530 introduces new requirements for situations when certain gains and losses (“other comprehensive income”) must be temporarily presented outside of net income in a new Statement of Comprehensive Income. Comprehensive income is the change in the Partner’s equity that result from transactions, events and circumstances from sources other than the Partners.

Commencing in the quarter ended March 31, 2007, the Partnership recorded the reversal of unrealized losses on derivative instruments outstanding at December 31, 2006 in other comprehensive income. These derivative instruments had previously been accounted for as cash flow hedges and recorded in accordance with hedge accounting.

In accordance with the transitional provisions, the Partnership has transferred the balance of deferred financing costs relating to the credit facilities and long-term debt entered into on November 30, 2006 to Partners’ equity at January 1, 2007.

On a prospective basis the Partnership will expense all financing costs.

#### *Asset Retirement Obligations*

In accordance with the Canadian Institute of Chartered Accountants’ Handbook Section 3110 “Asset Retirement Obligations”, the Partnership recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred when a reasonable estimate of fair value can be made and a legal obligation exists. The asset retirement costs equal to the fair value of the retirement obligations are capitalized as part of the cost of the related long-lived asset and allocated to amortization expense on a basis consistent with the expected useful life of the related asset. The liability is increased or accreted to full value with the passage of time based on the credit adjusted risk free rate with a periodic accretion expense charged to operating income. The liability may also be adjusted for revisions to the timing or amount of the original estimate of undiscounted cash flows to discharge the liability.

#### **NEW ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED**

The CICA has issued three new standards that may affect the financial disclosures and results of operations of the Partnership for interim and annual periods beginning January 1, 2008. The Partnership will adopt the requirements commencing in the interim period ended March 31, 2008 and is considering the impact this will have on the Partnership’s financial statements.

#### *Section 1535 – Capital Disclosures*

This Section establishes standards for disclosing information about an entity’s capital and how it is managed. Under this standard the Partnership will be required to disclose the following, based on the information provided internally to the entity’s key management personnel:

- (i) qualitative information about its objectives, policies and processes for managing capital;
- (ii) summary quantitative data about what it manages as capital;
- (iii) whether during the period it complied with any externally imposed capital requirements to which it is subject;
- (iv) when the Partnership has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

### Section 3031 - Inventories

This Section prescribes the accounting treatment for inventories and provides guidance on the determination of costs and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

### Section 3862 – Financial Instruments – Disclosures

This Section requires entities to provide disclosure of quantitative and qualitative information in their financial statements that enable users to evaluate (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and management's objectives, policies and procedures for managing such risks. Entities will be required to disclose the measurement basis or bases used, and the criteria used to determine classification for different types of instruments.

The Section requires specific disclosures to be made, including the criteria for:

- (i) designating financial assets and liabilities as held for trading;
- (ii) designating financial assets as available-for-sale; and
- (iii) determining when impairment is recorded against the related financial asset or when an allowance account is used.

### 4. Inventories

(millions of dollars, unaudited)	December 31, 2007	December 31, 2006
Pulp	63.7	48.9
Paper	14.0	11.6
Wood chips	10.7	5.4
Processing materials and supplies	48.4	45.1
	<b>136.8</b>	111.0

### 5. Property Plant and Equipment

(millions of dollars, unaudited)	December 31, 2007		
	Cost	Accumulated amortization	Net
Land and improvements	14.5	-	14.5
Buildings, machinery and equipment	1,294.7	726.8	567.9
Construction in progress	3.2	-	3.2
	<b>1,312.4</b>	<b>726.8</b>	<b>585.6</b>

(millions of dollars, unaudited)	December 31, 2006		
	Cost	Accumulated amortization	Net
Land and improvements	5.4	-	5.4
Buildings, machinery and equipment	1,272.6	684.5	588.1
Construction in progress	5.1	-	5.1
	<b>1,283.1</b>	<b>684.5</b>	<b>598.6</b>

## 6. Deferred Charges and Other Assets

(millions of dollars, unaudited)	December 31, 2007	December 31, 2006
Pension benefit plan (note 7)	11.3	-
Maintenance shutdown costs	1.4	3.0
Other	0.2	2.0
	12.9	5.0

## 7. Employee Future Benefits

The Partnership, in participation with Canfor, has funded and unfunded defined benefit plans, as well as a defined contribution plan, that provide pension, other retirement and post-employment benefits to substantially all salaried employees and for its hourly employees covered under collective agreements. The defined benefit plans are based on years of service and final average salary. The post-employment benefit plans are non-contributory and include a range of health care and other benefits.

Total employee future benefit expenses were as follows:

(millions of dollars, unaudited)	3 months ended December 31		Year ended December 31	
	2007	2006	2007	2006
Pension plans	1.2	1.0	4.8	4.4
Other employee future benefit plans	1.5	1.5	6.1	6.4
Contributions to forest industry union plans	1.3	1.2	6.3	6.2
	4.0	3.7	17.2	17.0

## 8. Asset Retirement Obligations

(millions of dollars, unaudited)	Year ended December 31, 2007
Balance beginning of period	-
Accrued obligation – ash pond	2.4
Accrued obligations - landfills	8.9
Accretion expense	0.1
Current expenditures	(0.3)
Change in estimate	0.2
Balance end of period	11.3
Less current portion	(2.1)
Long-term portion	9.2

During the third quarter of 2007, the Partnership recognized asset retirement obligations in respect of landfill closure costs. This reflects new information on all sites concerning the estimated timing of closure and closure alternatives. The obligations represent estimated future payments of \$20.1 million. Payments relating to landfill closure costs are expected to occur at periods ranging from 10 to 25 years which have been discounted at 5.8% and 6.3% respectively. The current estimated fair value is \$9.2 million and the amount is included in long-term liabilities.

During the second quarter of 2007 an environmental containment liability was identified at the Intercontinental mill site arising from the normal operation of the ash pond. As a result, the Partnership recorded an obligation based on the fair value of the containment estimate of \$2.4 million, with a corresponding capital addition to the related asset. The ash pond was decommissioned and remediation work commenced in the fourth quarter. The current estimated fair value was reduced by \$0.3 million to \$2.1 million after current period spending on remediation.

The Partnership has certain assets that have indeterminate useful lives and, therefore, there is an indeterminate settlement date for the related asset retirement obligation. As a result, no asset retirement obligations are recorded for these assets. These assets include, for example, wastewater and effluent ponds that will have to be drained once the related operating facility is closed and storage sites for which removal of chemicals and other related materials will be required once the related operating facility is closed. Once the useful life of these assets becomes determinable and an estimate of fair value can be made, an asset retirement obligation will be recorded.

## 9. Long-term Debt

At December 31, 2007 the Partnership has outstanding long-term debt of \$108.7 million (US\$110.0 million) in the form of unsecured U.S. dollar private placement notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013.

The fair value of long-term debt at December 31, 2007 was \$114.2 million (US\$115.6 million).

## 10. Long-term Liabilities

(millions of dollars, unaudited)	December 31, 2007	December 31, 2006
Accrued pension obligations (note 7)	4.3	3.0
Post employment benefits (note 7)	35.6	30.2
Derivative financial instruments	0.8	-
Asset retirement obligations (note 8)	9.2	-
	<b>49.9</b>	33.2

## 11. Related Party Transactions

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2006 audited consolidated financial statements and are based on agreed upon amounts which are intended to be market value, and are summarized below:

(millions of dollars, unaudited)	3 months ended December 31		Year ended December 31	
	2007	2006	2007	2006
<b>Transactions</b>				
Canfor	35.7	31.8	144.8	101.8
Howe Sound Limited Partnership - commission	0.6	0.7	2.9	4.7
Howe Sound Limited Partnership - purchase of wood chips	0.7	-	0.7	-
Lakeland Mills Ltd. and Winton Global Lumber Ltd. – purchase of wood chips	1.9	2.7	11.5	8.6
			<b>December 31</b>	
			<b>2007</b>	<b>2006</b>
<b>Balance Sheet</b>				
Included in accounts payable and accrued liabilities:				
Canfor			30.8	20.9
Howe Sound Limited Partnership			35.0	23.1
Lakeland Mills Ltd. and Winton Global Lumber Ltd.			0.3	0.8
Included in trade accounts receivable:				
Product marketed for Canfor			14.2	6.3
Product marketed for Howe Sound Limited Partnership			31.8	31.9

Transactions and payables to Canfor include purchases of wood chips, pulp and administrative services.

## 12. Income per Partnership Unit

Basic income per Partnership unit is based on the weighted average number of Limited Partnership units outstanding during the period. All outstanding Partnership units were issued on July 1, 2006, and there was no change in the number of outstanding Partnership units during the quarter. For purposes of comparative amounts for periods prior to July 1, 2006, it was assumed that the same number of units was outstanding throughout the comparative periods. There were no other securities with rights to conversion into Partnership units outstanding.

## 13. Financial Instruments

The Partnership uses a variety of derivative instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, pulp prices and natural gas.

For the three and twelve months ended December 31, 2007, the Partnership recorded realized losses of \$1.1 million (2006 – nil) and \$2.2 million (2006 – nil) respectively, on maturing commodity swaps hedging natural gas purchases as a charge to manufacturing and product costs. At December 31, 2007, the Partnership had outstanding commodity swaps hedging future natural gas purchases of 4.9 million gigajoules extending to October 2010. At December 31, 2007 the unrealized loss of \$2.7 million on these outstanding commodity swaps is recorded as a liability in accounts payable and accrued liabilities or long-term liabilities. For the year ended December 31, 2006, the Partnership had unrealized losses on outstanding natural gas swaps of \$0.8 million and pulp swaps of \$1.0 million. These instruments, which were previously recorded using hedge accounting, were measured at fair value on January 1, 2007 with a corresponding adjustment through other comprehensive income (see notes 3 and 16).

## 14. Supplementary Cash Flow Information

(millions of dollars, unaudited)	3 months ended December 31		Year ended December 31	
	2007	2006	2007	2006
<b>Changes in non-cash working capital</b>				
Accounts receivable	(3.0)	23.9	(18.1)	0.3
Inventories	(5.0)	(11.2)	(25.8)	(4.0)
Prepaid expenses	6.9	4.2	(2.5)	(8.2)
Accounts payable and accrued liabilities	(22.2)	(17.9)	21.4	1.4
	(23.3)	(1.0)	(25.0)	(10.5)
<b>Capital expenditures</b>				
Capital expenditures – cash	11.5	5.1	23.8	19.6
Capital expenditures – accruals	3.2	-	8.1	-
Asset retirement obligations – long-term	0.2	-	9.1	-
	14.9	5.1	41.0	19.6
<b>Net interest paid</b>	<b>3.0</b>	<b>2.6</b>	<b>6.8</b>	<b>2.5</b>

## 15. Distributions

The Partnership declared distributions in the twelve months of 2007 as follows:

(millions of dollars, except per unit amounts, unaudited)			
Record Date	Payable Date	Amount per Partnership Unit \$	Amount \$
January 31, 2007	February 15, 2007	0.14	10.0
February 28, 2007	March 15, 2007	0.14	9.9
March 30, 2007	April 13, 2007	0.14	10.0
April 30, 2007	May 15, 2007	0.14	10.0
May 31, 2007	June 15, 2007	0.18	12.8
June 29, 2007	July 13, 2007	0.18	12.8
July 31, 2007	August 15, 2007	0.18	12.8
August 31, 2007	September 14, 2007	0.18	12.9
September 28, 2007	October 15, 2007	0.18	12.8
October 31, 2007	November 15, 2007	0.14	10.0
November 30, 2007	December 14, 2007	0.12	8.5
December 31, 2007	January 15, 2008	0.12	8.6
		1.84	131.1

## 16. Accumulated Other Comprehensive Income

(millions of dollars, unaudited)	3 months ended December 31, 2007	Year ended December 31, 2007
Balance, beginning of period	0.6	-
Accounting policy change for derivative instruments:		
Unrealized loss on natural gas swaps	-	(0.8)
Unrealized loss on pulp swaps	-	(1.0)
Balance, beginning of period, as restated	0.6	(1.8)
Adjustment for derivatives recorded in other comprehensive income	(0.1)	2.3
Balance, end of period	0.5	0.5

The total of the net income, accumulated other comprehensive income, less distributions is as follows:

(millions of dollars, unaudited)	December 31, 2007
Cumulative net income	216.5
Cumulative distributions	(219.6)
Accumulated other comprehensive income	0.5
	(2.6)
Partners' capital – at July 1, 2006, as restated	587.5
Partner's equity, end of period	584.9

## 17. Segmented Information <sup>(a)</sup>

(millions of dollars, unaudited)	Pulp	Paper	Unallocated Costs <sup>(d)</sup>	Total
<b>3 months ended December 31, 2007</b>				
<b>Sales to external customers <sup>(b)</sup></b>	<b>186.0</b>	<b>29.1</b>	<b>-</b>	<b>215.1</b>
<b>Sales of pulp to paper segment <sup>(c)</sup></b>	<b>18.9</b>	<b>(18.9)</b>	<b>-</b>	<b>-</b>
<b>Operating income (loss)</b>	<b>16.0</b>	<b>(0.9)</b>	<b>(3.4)</b>	<b>11.7</b>
<b>Amortization</b>	<b>13.6</b>	<b>1.1</b>	<b>0.1</b>	<b>14.8</b>
<b>Capital expenditures, net</b>	<b>14.5</b>	<b>0.3</b>	<b>0.1</b>	<b>14.9</b>
3 months ended December 31, 2006				
Sales to external customers <sup>(b)</sup>	194.3	30.9	-	225.2
Sales of pulp to paper segment <sup>(c)</sup>	20.1	(20.1)	-	-
Operating income (loss)	47.7	1.7	(3.8)	45.6
Amortization	11.5	1.0	0.1	12.6
Capital expenditures, net	4.5	0.6	-	5.1
<b>Year ended December 31, 2007</b>				
<b>Sales to external customers <sup>(b)</sup></b>	<b>798.0</b>	<b>123.6</b>	<b>-</b>	<b>921.6</b>
<b>Sales of pulp to paper segment <sup>(c)</sup></b>	<b>79.9</b>	<b>(79.9)</b>	<b>-</b>	<b>-</b>
<b>Operating income (loss)</b>	<b>152.6</b>	<b>(2.1)</b>	<b>(16.2)</b>	<b>134.3</b>
<b>Amortization</b>	<b>48.5</b>	<b>4.1</b>	<b>0.2</b>	<b>52.8</b>
<b>Capital expenditures, net</b>	<b>39.1</b>	<b>1.8</b>	<b>0.1</b>	<b>41.0</b>
<b>Identifiable assets</b>	<b>813.0</b>	<b>71.9</b>	<b>24.1</b>	<b>909.0</b>
Year ended December 31, 2006				
Sales to external customers <sup>(b)</sup>	717.1	113.3	-	830.4
Sales of pulp to paper segment <sup>(c)</sup>	71.4	(71.4)	-	-
Operating income (loss)	143.8	1.7	(14.3)	131.2
Amortization	45.0	3.8	0.2	49.0
Capital expenditures, net	17.0	0.8	1.8	19.6
Identifiable assets	784.1	70.8	38.8	893.7

- (a) Operations are presented by product lines. Operations are considered to be in one geographic area since all production facilities are in Canada. Substantially all sales are exported outside Canada, with sales to the United States representing 44% (2006 – 41%).
- (b) Sales to the largest customer represented approximately 24% of pulp segment sales (2006 – two largest customers - 36%).
- (c) Sales of slush pulp to the paper segment are accounted for at approximate market value. The sales are transacted as a cost transfer and are not reflected in Pulp sales.
- (d) Unallocated costs represent actual head office administrative costs in 2007. For the first six months of 2006, head office administrative costs were based on allocated Canfor corporate expenses as described in Note 1.

## 18. SUBSEQUENT EVENT

On January 15, 2008 a fire at the Partnership's Prince George Pulp and Paper mill caused extensive damage to the chip screening and infeed system. Alternative chip screening and infeed systems are being investigated to minimize pulp production disruptions at this mill. The Partnership has property damage and business interruption insurance to limit the financial loss to the Partnership. The occurrence is not expected to have a material effect on the financial condition of the Partnership.