FINAL TRANSCRIPT

Canfor Corporation

Canfor and Canfor Pulp First Quarter Analyst Call

Event Date/Time: April 26, 2018 — 10:30 a.m. E.T.

Length: 25 minutes

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PRESENTATION

Operator

Good morning, ladies and gentlemen. Welcome to the Canfor and Canfor Pulp First Quarter Analyst Call.

A recording and transcript of the call will be available on Canfor's website.

During this call, Canfor and Canfor Pulp's Chief Financial Officer will be referring to a slide presentation that is available in the Investor Relations section of each company's website. Also, the companies would like to point out that this call will include forward-looking statements, so please refer to the press releases for the associated risks of such statements.

I would now like to turn the meeting over to Mr. Don Kayne, Canfor and Canfor Pulp's Chief Executive Officer. Please go ahead, Mr. Kayne.

Don Kayne — President and Chief Executive Officer, Canfor Corporation

Thank you, Operator, and good morning, everyone. Thank you for joining the Canfor and Canfor Pulp Q1 2018 results conference call this morning. I'll make a few comments before I turn things over to Alan Nicholl, our Chief Financial Officer for both Canfor Corporation and Canfor Pulp. Alan will provide a more detailed overview of our performance in Q1.

In addition, I want to congratulate Alan on his new expanded role as Executive Vice President of Pulp Operations. I know Alan is excited about working even more with the Canfor Pulp team.

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Joining Alan and I today are: Peter Hart, Vice President of Pulp Sales; Kevin Pankratz, Senior Vice President of Lumber Sales and Marketing; and Stephen Mackie, Senior Vice President of Canadian Operations.

Before I get into the quarter, I wanted to take a minute to comment on some of the record results from 2017 which I discussed at our Annual General Meeting yesterday. Across the Company, we achieved our safest year ever for the second consecutive year. Our medical incident rate was 1.68, and a number of our operations were recognized by industry and safety organizations for their excellent safety records.

Canfor produced and shipped a record number of prime products in 2017, both in Spruce/Pine/Fir and Southern Yellow Pine. Our capital investments and disciplined cost management led to higher productivity, offsetting extreme weather conditions in many locations, including significant rainfall, wildfires, and hurricanes.

Canfor set a record for total sales. And thanks to the stronger lumber and pulp market prices, we had the highest operating income since 2004. Our consolidated operating income was $557 million, which was up 82 percent from 2016.

At the end of 2017, our net debt to capitalization was 4.6 percent, which was the lowest since 2010. This reflected our strong cash earnings and debt reduction focus.

Now turning to our Q1 results, beginning with Canfor Pulp. The Company generated another record high quarterly operating income of $85 million in the quarter, surpassing the previous high set

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last quarter by 18 million. The Company also set a record for sales, with $300 million recorded in the quarter.

Demand for pulp continued the trend from the end of 2017 and was very strong throughout the quarter, holding at near-record prices. Pulp shipments were impacted by transportation challenges in the quarter, but 14,000 tonnes of product that were not shipped in Q4 were delivered in the quarter, mitigating the impact to a large degree.

In the second quarter, we will be taking normal maintenance outages at a number of our mills, which will reduce our production by 11,000 tonnes of BCTMP, 5,000 tonnes of NBSK, and 4,000 tonnes of paper. Strong demand in the traditional spring maintenance season currently underway continued to support excellent pricing in the second quarter. Looking towards the back half of the year, while we continue to be cautious about incremental pulp supply, we are more optimistic than we were a few months ago regarding the future supply-demand balance.

Moving to the lumber business. Our operations faced significant weather challenges which negatively impacted production in the quarter. At the same time, there were major transportation challenges that significantly impacted our ability to ship product on time, and as a result, also negatively impacted our results. However, North American demand remains strong, and supply constraint kept prices high through most of the quarter, more than offsetting the impact of duties paid, which were finalized at the end of 2017.

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Offshore markets were strong, with another record year in Japan in 2017, and we continue to focus on improving our higher value sales mix into these regions as our supply of low-grade product from British Columbia continues to decrease.

Our outlook for 2018 is for continued incremental demand in the United States, which will more than offset announced supply increases in the US South and the net imports from Europe. In regard to our previously announced greenfield mill, we continue to work to resolve the contractor issue, and at this point, we cannot give clear guidance on the timetable, other than to say construction will commence in the first half of 2019, with expected start-up in 2020.

I will now turn it over to Alan to provide an overview of our financial results.

Alan Nicholl — Chief Financial Officer and Executive Vice President, Finance and Canfor Pulp Products Inc., Canfor Corporation

Well thanks, Don, and good morning, everyone. As usual, my comments this morning will focus principally on our financial performance for the first quarter of 2018 by reference to the previous quarter. Full details of our results are contained in the Canfor Pulp and Canfor news releases, both of which were issued on Tuesday evening.

As always, you'll find an overview slide presentation on both the Canfor and Canfor Pulp websites, in the Investor Relations section under Webcasts. The presentation highlights consolidated and segmented results, and I'll be referring to this presentation during my comments.

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For the first quarter of 2018, Canfor reported shareholder net income of $112 million, or $0.87 a share, down from net income of $132 million, or $1.02 a share, reported for the fourth quarter, and up from net income of $66 million, or $0.50 a share, reported for the first quarter of 2017.

On Slide 3 of our presentation, we highlight various nonoperating items, net of tax and noncontrolling interests, which affect the comparability of our results between the quarters. In the first quarter of 2018, added-back expenses totalled $33 million, the largest relating to countervailing and anti-dumping duty deposits of $26 million, in contrast to a $17 million ADD recovery recorded in Q4 relating to a true-up of duties to current period rates.

After adjusting for the aforementioned items, shareholder net income for Q1 2018 was $145 million, or $1.13 a share, up $30 million compared to $115 million, or $0.89 a share, for the fourth quarter.

As highlighted on Slide 5 of our presentation, Q1 operating income for the lumber segment was $126 million, down $29 million from the previous quarter. The decrease reflected increased duty deposits recorded in the current quarter, with both CVD and ADD in effect for the full period following the reintroduction of CVD deposits in late December.

As previously noted, results in the prior quarter included an ADD recovery for current period rates. After adjusting for the impact of duties, Q1 operating income was $161 million, and that was up 29 million from the $132 million recorded for Q4 2017.

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US housing starts were up by an average of 5 percent from the previous quarter, principally reflecting an increase in multifamily starts, while Canadian housing starts were consistent with the previous quarter, and offshore markets remained solid. Lumber sales realizations showed a modest improvement as higher US-dollar SPF and Southern Yellow Pine lumber prices outweighed the impact of the increased duties.

Unit manufacturing costs in the current quarter showed a small increase for stable logs and productivity gains at our Southern Pine operations, largely offsetting increased market-based stumpage and purchased-wood costs north of the border, as well as the effects of the weather challenges in Western Canada that Don referred to, which caused significant disruption to our operations.

Canfor's pulp and paper segment comprises the results of Canfor Pulp Products Inc. And as highlighted on Slide 6, the Company reported a record-high net income of $64 million, or $0.99 a share, in Q1 compared to net income of $45 million, or $0.69 a share, for the fourth quarter. Adjusted shareholder net income for Q1 was $64 million, and $0.99 a share, and that was up $16 million, or $0.26 from the fourth quarter.

As Slide 7 highlights, Canfor Pulp's Q1 financial performance reflected continued strong global softwood pulp markets with NBSK prices holding at near-record highs. Our pulp shipments were up 3 percent from the previous quarter as the benefit of a 14,000-tonne shipment slippage from

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late December into January more than offset the weather-related transportation constraints in the current quarter.

Pulp production was broadly in line with the previous quarter, as increased operating days and a strong production performance in March offset various weather-related disruptions in January and February. Unit manufacturing costs were moderately higher than previous quarter, in large measure due to market-driven increases in fibre costs and weather-related increases in energy costs.

Operating income for the paper segment in Q1 was $3 million, down 4 million from the previous quarter, as a modest increase in sales realizations was offset by market-related increases in slush pulp costs and the timing of shipments.

Capital spending in the first quarter of 2018 totalled approximately $56 million and included $36 million in the lumber business and $20 million in Canfor Pulp. For 2018, before taking account of our previously announced greenfield development, we currently anticipate capital spending for lumber will be in the region of $240 million and $90 million for pulp. The timing of the spend on our greenfield site now looks likely to occur in 2019 and early 2020.

Consistent with the prior quarters, Canfor Pulp's Board of Directors approved the continuance of a quarterly dividend of $0.0625 per share for the first quarter. And at the end of Q1, Canfor is splitting Canfor Pulp with net debt of $216 million, with available liquidity of 358 million. Canfor Pulp had net cash of just under $120 million, with available liquidity of 99 million. Net debt to

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total capitalization, excluding Canfor Pulp, was 10.3 percent, and on a consolidated basis was 4.3 percent.

And with that, Don, I'll turn the call back over to you.

Don Kayne

All right. Thanks, Alan. And so, Operator, we're now ready to take calls from analysts.

Q&A

Operator

Thank you. We will now take questions from financial analysts. If you have a question, please press *, 1 on your telephone keypad. If you are using a speakerphone, please lift your receiver and then press *, 1. If at any time you wish to cancel your question, please press *, 2. Please press *, 1 now if you have a question. There will be a brief pause while participants register. Thank you for your patience.

Your first question comes from Sean Steuart from TD Securities. Sean, please go ahead.

Sean Steuart — TD Securities

Thanks. Good morning, everyone.

Don Kayne

Good morning, Sean.

Sean Steuart

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A few questions. Good morning. A few questions and I'll start with freight. One of your competitors suggested that Canadian freight constraints affected their Q1 EBITDA by about 40 million. Do you have an estimated impact on your profitability for the quarter?

Don Kayne

For sure, Sean. I mean, clearly, we saw significant issues through the quarter as well, first of all, as you no doubt would know. And from our standpoint, I mean there's several parts to it, but overall if you look at the hard and the soft costs combined, we're somewhere in the neighbourhood of $20 million, would be our best guess. And depending on what the markets do down the road here and how quickly we are at reducing our inventory levels, it could go, obviously, much higher. But for now, that's the number that we think we've been impacted for, during Q1.

Sean Steuart

Okay. Thanks, Don. And I mean, notwithstanding those headwinds, it looks like your Q1 Western Canadian lumber shipment trends actually held up relatively well versus West Fraser's and what we would have seen for general industry trends. Can you give any context on measures you'd take to circumvent those restrictions and get around it where you can?

Don Kayne

Yeah. Well, I mean I think we certainly saw, despite the fact that there's some areas we did fairly well at, but we also had significant issues through the quarter. And just, I mean, we should have shipped a lot more than we did. Our inventories at our mills increased significantly, both on the

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finished product on our sawmills, and in our pulp mills we had inventory outside for much of the quarter on the pulp side. And then on the lumber side, our inventory, to give you an idea, was up—on our dressed side at our mills was up over 50 percent of normal through the quarter, so it was a significant issue for us.

And the other thing that we don't talk about too much but it's a big one, and it's hard to measure, and it's one that we're pretty passionate about, is the impacts that all these transportation issues are having on our Canadian brand and our BC brand. Because if you look at it around the world, we're competing more than ever with concrete and steel, but also with the Europeans and Yellow Pine and everything else. And we've got so many things facing us that it's not good when we suffer the kind of reliability issues that we face as an industry.

So I think we're all working hard on this, jointly, trying to share best practices as best as we can, but it's a big issue for us as well. I mean, that maybe—gives you a little more colour there.

Sean Steuart

Yeah. Definitely. And one more question, then I'll get back in the queue. Do you have any visibility from CN and the rest of your providers on when availability is expected to loosen up? And any visibility, I guess, on unwinding your finished product inventory?

Don Kayne

Yeah. No. For sure. Well, I can assure you that it's something that all of our folks, our transportation and logistics and supply chain folks for sure, and also our operations folks as well, are

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in daily contact with the railroads. And they've been super-communicative and understand the issues that we're all facing. And so our—at this point, we are making progress. Weather's improved, obviously, significantly from where it was in the first part of the year.

And so we're seeing some relief on the pulp side particularly, which we're expecting to be out from some of the issues by the end of Q2. And then on the lumber side, while there's some optimism that it might be somewhere in that same area, our view, or my view, would be that it will take a little bit longer than that, maybe an extra couple of months beyond that.

And then in terms of the residual side, that's really where we have a bit of an unknown there, and that's the chips at some of our sawmills which is significantly high. And we're concerned about that, long term, because residual chips, the more you leave them around, the more likelihood you're going to get some degradation, and of course, that's going to impact the cost and recovery and so forth down the road, right? So that subject, which is really more boxcar-related, is going to be–and hovercar, I guess, related—is going to be probably more towards the end of the year before we get out from under that. That's our best guess.

Sean Steuart

Okay. Thanks very much for that, Don. I'll get back in the queue.

Don Kayne

Okay. Thanks, Sean.

Operator

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Thank you. Your next question is from Paul Quinn from RBC Capital Markets. Paul, please go ahead.

Paul Quinn — RBC Capital Markets

Yeah. Thanks very much. Good morning, guys.

Don Kayne

Good morning, Paul.

Paul Quinn

Hey, just to hammer you on this transportation issue. From listening to you, it sounds like a huge deal for you in the quarter, and it probably was. But when I look at the end results, I mean you really only built 38 million in inventory in Western SPF volumes and only 6 million in the Southern Yellow Pine. I mean, that's like 4 percent inventory build versus 20 percent for West Fraser. So I'm just wondering, have you got less exposure to CN than West Fraser does overall? What is the big difference? Because if I look back in the past, I mean, you guys have generally built less inventory. If I go back to '14, which was a terrible year in Q1, I mean West Fraser built 27; you built 20. So just wondering what the big overall difference is there? Just so I can understand it.

Don Kayne

Yeah. I mean, well, partly, our production was off a little bit for starters, okay, so compared to where it normally is, which probably eased a bit of that. I guess the other made it look maybe a bit better, but still, that's still a big number for us, right, that we're not happy about at all.

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But I think also, though, I would comment on just what we've—we've invested, as you know, a ton of dollars here in terms of our supply chain and our systems and so forth. And I think that—I think we'd like to say at least that some of that is certainly paying off in a good way, and we'll continually get better at that. But CN's a big, big part of our business. I mean, we don't have all that many mills, maybe one—maybe just one or maybe two, but. And actually, there's one mill only that's on the CP. So at the end of the day, our production has been off, which made it look a little bit better.

But also, we've invested heavily in the supply chain overall because it's such a critical piece of our business, because we sell so much of our product direct to the end user. And so that's really, was—when you think back three, four, five years—that's why we invested heavily going back that many years, and we're hopefully seeing some of the benefits of that today.

Paul Quinn

No. It's a huge benefit relative of performance; it's very impressive. So if I could—one of the things that a lot of investors bring up with the high Western SPF prices right now is they're high because of the transportation constraints. And it looks like you weren't as constrained. What do you think of the rest of the industry? And do you think that's a fair comment on the high pricing?

Don Kayne

For sure. I mean, high pricing gets blamed on a lot of things, but—softwood lumber to start with and all that, duties, and then now in transportation. And there's no question that both had and

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are having an impact for sure. I think particularly the transportation, really since October, is having an impact for sure.

But also, though, if you really—and I've had a chance, a number of chances, to travel around a bit here in the last while, overseas and in Europe as well. And if you really go between the retail business, which continues to be real, real strong, and maybe, Kevin, you can touch on that in a second here later.

And also, the new home construction continues to move gradually up; you know we're over 1.3. Then you look in Japan; again, Paul, we had a record year in 2016, another one in 2017. China's staying relatively stable, if you consider the higher-value products that are being shipped over there. In Europe, they're really, really strong there, as well—more than what most of the big companies would've expected there.

And then you factor in, on terms of supply in the world—there's really only one area that we're going to see any increases, and that's in the Southern Yellow Pine. Europe, they're not going to increase; it'll be flat. We know what's happening in Western Canada. And in Eastern Canada, it's not going up any time fast either, really, of any magnitude. So I think all of that played a bit of a role in it.

And then the whole factor around new applications, which we tend not to talk about, but around the mid-rise, particularly, three and four and five-to-seven-storey, and as well as some of the tall buildings. So if you factor all that in, I think that really all bodes well for the longer term, but it's

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also had a big impact too, aside from transportation. So long-winded, but I thought it just important to mention that.

Paul Quinn

No. It's really helpful. And then maybe just switching over to Pulp. You made an executive change in the quarter. Just want to—what the impetus with that was? And then sort of an outlook—looks like Q2 seems pretty stable to Q1, maybe a slight increase on price, but offset by the maintenance. What do you think for the back half for the year?

Don Kayne

Peter, why don't—you're the pulp marketing expert here. Why don't you talk and give Paul a bit of a view on with how you see the markets here, going forward?

Peter Hart — Vice President, Pulp and Paper Sales, Canfor Corporation

Certainly as we look at the back half of the year, we remain uncertain. There's still some capacity to come onstream in the second quarter, and there's ramp-ups from last year. Having said that, though, the overall supply-demand balance for the next three years is projected to be higher than we would've expected even a few months ago. So while we're cautious, we are more optimistic than we were.

Paul Quinn

Okay. And then, Don, can you—

Don Kayne

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And then—well, the first part—

Paul Quinn

—change in the management change?

Don Kayne

Yeah. On your first part of the question there, I'll maybe give you a bit of colour there briefly. First of all, I would say Brett was a terrific—contributed to the Company over several years for sure. And as I did at the AGM yesterday, I wanted to recognize and thank him for all his contributions. Definitely had a good impact on the Company over many years.

I guess in a—what I thought, and you've kind of known, or at least I think we've been fairly vocal of it for awhile. I really saw an opportunity overall to really bring these companies, Canfor and Canfor Pulp, even closer together than what they might have been in the past. And we've made some good progress there, but I felt that there was a real opportunity there to bring it even closer. And so with Alan's background in Pulp, going back several years, he's well-versed in the business.

And then the strong management team that we have, with Peter, who you guys have all spoken to and are aware of, as well as Martin Pudlas, who's a VP of Operations in the North for the pulp mills. And then we've got some strong management underneath that as well at the pulp mills, particularly, overall, right? So if you look at it across the organization, I just felt that it was a time to do that and make that change. And so those are, I guess—that maybe adds a little bit of colour for you.

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Paul Quinn

Good. Thanks very much. Best of luck.

Operator

Thank you. Your next question is from Hamir Patel from CIBC Capital Markets. Hamir, please go ahead.

Hamir Patel — CIBC Capital Markets

Hi. Good morning.

Don Kayne

Good morning.

Hamir Patel

Don, could you comment on maybe how long your order files are, on the lumber side? And also, how much of your business is currently priced at the time of shipment versus the time you book the order? And how do the dynamics typically work if, say, prices were to come off in the back half of the year? How that would affect realizations?

Don Kayne

For sure. Maybe I'll let Kevin speak to that. Kevin, maybe give Hamir an idea about those?

Kevin Pankratz — Senior Vice President of Lumber Sales and Marketing, Canfor Corporation

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Sure. Hamir, maybe I'll just break it down in a couple of different ways. So in our North American order file, we actually do have a fairly strong one that's extending into May, which gives us pretty good confidence that the prices are going to remain relatively strong into the second quarter.

And then for the offshore markets, we tend to book that more on a monthly basis, so we have a fairly good commitment order file in Japan and into China. So from all three markets there, we've probably got the strongest order file as an entity, compared to last couple years, is pretty strong.

Hamir Patel

Okay. And then—

Kevin Pankratz

And then as far as the—as far as the pricing component goes there, with the three to four-week cash order file, I mean, those are commitments. But then you also know we're fairly active in the R&R segment and where we have contracts that are based on the timed shipments. So that piece there would be relatively current, based on what the weekly pricing is doing and just aligned with that, weekly takeaway.

Hamir Patel

Got it. No, that's helpful. So how much of the overall mix is big-box?

Don Kayne

Probably in the neighbourhood of a fifth of—what—our business?

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Kevin Pankratz

Yeah. About—yeah. About 20 percent, 22 percent.

Hamir Patel

Okay. Thanks. That's helpful. And, Don, on the greenfield. Is the location and capacity still going to be the same? Or is that still subject to change, depending on the equipment vendor?

Don Kayne

Location's the same, volume's the same. And regardless on what vendor we use, Hamir, that's the location that we believe's the right location. And the volume that we've talked about was certainly the number that we think's valid, going forward.

Hamir Patel

Great. Thanks, Don. That's all I had. I'll turn it over.

Don Kayne

Okay. Thanks, Hamir.

Operator

Thank you. There are no further questions. I will now turn it back over for closing remarks.

Don Kayne

All right. Thanks very much, Operator, and thanks very much, everyone, for joining our Q1 call. I appreciate all the questions, and we look forward to the next quarter call. Thanks.

Operator

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Ladies and gentlemen, this concludes today's conference call. We thank you for participating, and we ask that you please disconnect your lines.

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