

FINAL TRANSCRIPT

Canfor Corporation

Canfor and Canfor Pulp Fourth Quarter Analyst Call

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PRESENTATION

Operator

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

A recording and transcript of the call will be available on the Canfor and Canfor Pulp websites.

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 — Chief Executive Officer, Canfor Corporation

Thank you, Operator, and good morning, and thank you for joining the Canfor and Canfor Pulp Q4 2016 results conference call.

I'll make a few comments about the quarter and our outlook before I turn things over to Alan Nicholl, Chief Financial Officer for both Canfor Corporation and Canfor Pulp. Alan will provide a more detailed overview of our performance in Q3—or Q4, actually, after which we will take questions.

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In addition to Alan, on the line with me today are Brett Robinson, President of Canfor Pulp; Peter Hart, Vice President of Pulp Sales; and Wayne Guthrie, Senior Vice President of Lumber Sales and Marketing.

Starting with Canfor Pulp. The mills ran well in the quarter, but challenging weather in December impacted production and shipments as some vessels slipped into January.

Demand from China continues to be strong, and pricing has been moving higher in all markets. Global softwood demand is positive for both NBSK and BCTMP, and we expect this to continue through the second quarter as we begin the spring maintenance season.

For our lumber operations, weather throughout our operating areas impacted our fourth quarter results. That being said, through the considerable efforts of our teams we saw strong improvement in our financial performance over the course of 2016.

Our key offshore markets remain steady, and inventory levels are low, particularly in China. We expect solid demand throughout 2017.

The North American housing market continues its gradual but steady recovery, and we expect the repair and remodelling sector to continue the significant growth witnessed over the last number of years. Overall, we forecast US consumption of softwood lumber to increase by approximately 2 billion feet in 2017 on top of the over 2 billion foot increase in 2016.

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Early in January 2017 we completed the final phase of our purchase of Beadles and Balfour Lumber Company, acquiring the remaining 45 percent of that business. This completes the last of our phased purchase commitments.

Finally, I will end with comments on softwood lumber agreement. As you know, the US Department of Commerce is proceeding with its investigation in response to the petition filed by the US coalition.

This was expected, as was the fact that Canfor as one of the largest exporters in the country was selected as a respondent for both CVD and ADD (sic) [AD] investigations. Negotiations for a new managed trade agreement will continue alongside these investigations, as will the Canadian government's defence of our industry against these unfounded allegations of subsidy.

In the meantime, our significant investments in our Canadian facilities, our focus on geographic market diversification, along with our strong mill network in the US South of 1.4 billion board feet, put us in a much stronger position than we were in previous rounds of softwood lumber disputes.

We will continue to focus on serving our customers in the US market and working with industry and government towards a resolution.

With that, I will turn the call over to Alan to provide an overview of our financial results.

Alan Nicholl — Chief Financial Officer, Canfor Corporation

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Well, thanks, Don, and good morning, everyone. As usual, my comments this morning will focus principally on our financial performance for the fourth quarter of 2016 by reference to the previous quarter. Full details of our results are contained in the Canfor Pulp and Canfor news releases which were issued yesterday afternoon.

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.

For the fourth quarter of 2016, Canfor reported shareholder net income of \$38 million, or \$0.29 a share, down from net income of \$51 million, or \$0.38 a share reported for the third quarter, and well up from net income of \$2 million, or \$0.01 a share reported for the fourth quarter of 2015.

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 respective quarters. In the fourth quarter of 2016 these items had a negligible impact on the reported earnings numbers.

Results for the lumber segment are highlighted on Slide 5 of our presentation. Operating income for the fourth quarter was \$57 million, an \$18 million decrease from operating income reported in the prior quarter.

As highlighted in our press release, the lower operating income in large part reflected weather-related challenges in Western Canada that impacted both log deliveries and productivity.

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Likewise, lower shipment and production volumes in the fourth quarter reflected the weather-related challenges, as well as additional stat holidays.

Western SPF lumber sales realizations showed a modest quarter-over-quarter increase, reflecting a 2 percent weaker Canadian dollar and a higher-value sales mix, while US Southern Yellow Pine sales realizations in US dollars reflected seasonal price declines for most wider grades, which more than offset an increase in the price of 2x4 #2 lumber.

Unit manufacturing costs were modestly higher than the previous quarter, again, primarily due to the aforementioned weather-related challenges and to a lesser extent seasonally higher energy costs.

Canfor's pulp and paper segment comprises the results of Canfor Pulp Products Inc. The Company reported net income of \$10 million, or \$0.15 a share, compared to net income of \$22 million, or \$0.34 a share, for the third quarter and net income of \$30 million, or \$0.43 a share, for the fourth quarter of 2015.

The net earnings for the current quarter included a \$5 million or \$0.08 a share write-down of advances made in connection with our biofuels technology initiative with Licella. Notwithstanding the future potential benefits that may result from this innovative venture, this prudent accounting treatment reflected the research and development nature of these advances.

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As you'll see on the summary of Canfor Pulp's operating results on Slide 7, similar to our lumber segment, the decrease in operating results in Q4 was primarily attributable to the disruption to operations and logistics costs by the challenging weather.

On the plus side, global softwood pulp markets were relatively stable through most of the quarter, with average NBSK pulp prices to China in line with those of the previous quarter. NBSK pulp sales realizations were largely unchanged.

BCTMP sales realizations showed healthy gains, reflecting stronger US dollar pricing, as well as the weaker Canadian dollar.

Shipments were down 14 percent from the prior quarter, primarily due to the lower NBSK production and a vessel shipment that slipped into early 2017. Higher unit manufacturing costs reflected the lower productivity, as well as seasonally higher energy costs.

Operating income for the paper segment in Q4 was \$8 million, up 1 million from the previous quarter, reflecting both the weaker Canadian dollar, as well as increased production.

Capital spending in the fourth quarter totalled \$63 million, of which 42 million was in the lumber business and 18 million in Canfor Pulp. 2017 capital spend is currently projected to be approximately \$165 million for Canfor and just over \$75 million for Canfor Pulp, that latter number including major maintenance.

Consistent with other quarters, Canfor Pulp's Board of Directors yesterday approved the continuance of a quarterly dividend of \$0.0625 per share.

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And as Don mentioned earlier, immediately after year-end on January 2nd Canfor completed the purchase of the remaining 45 percent of Balfour and Beadles at a cost of US\$31 million. This payment concludes all of the Company's phased purchase agreements.

At the end of the year, Canfor, excluding Canfor Pulp, had net debt of \$321 million with available liquidity of 330 million. Canfor Pulp had net cash of \$2 million with available liquidity of just over 100 million. Net debt to total cap, excluding Canfor Pulp was 17.5 percent, for Canfor Pulp it was 0, and on a consolidated basis it was just over 15 percent.

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

Don Kayne

All right. Thanks, Alan. So, Operator, we would now be ready to take questions.

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 for questions. Thank you for your patience.

Your first question comes from Ketan Mamtora from BMO. Please go ahead.

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Ketan Mamtora — BMO

Good morning.

Don Kayne

Good morning.

Ketan Mamtora

First question, and again to the extent that you can, but can you provide any kind of additional colour around kind of the ongoing negotiations? And is it still now with respect to quota is it kind of figuring out the middle ground? Or any update that you can provide will be helpful.

Don Kayne

Thank you for the question. I think there's not a lot more really than what I mentioned in the initial comments around the whole agreement. I think that—I guess the one positive is that there certainly is some negotiations and conversations going on. I think the federal government has been leading this, as they have been for some time now, and from what we understand we're pleased with the progress and the support that we're getting.

Maybe one comment I would make is—because it'll probably come up later—is around critical circumstances. That's the one thing that everyone's paying attention to. And ourselves around that subject we believe that we've—through the discipline that we've, I think, ourselves and others have exercised in terms of overseas shipments and other markets that from our standpoint we are not concerned around the threshold levels that would need to be in place.

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Canfor Corporation Canfor and Canfor Pulp Fourth Quarter Analyst
Call**Ketan Mamtora**

Got it. That's helpful. And, Don, is the level of quota still the main sticking point?

Don Kayne

Well, I think that the level of potentially level of market share is for sure at this point. And likely at the end of the day here it will continue to be the key sticking point or the key negotiation point.

Ketan Mamtora

I see. That's helpful. And then just switching to your Q4 lumber shipments, I was a little surprised they were down year over year. And I know you referenced some bit of weather issue, but anything else going on there and why they were down year over year?

Don Kayne

No, I think it really it's 100 percent associated with that. And we just had—it's hard to describe, but having seen several of the pictures of what our operations on both the pulp side, frankly, and the lumber side had to deal with through the quarter from severe weather, severe rain initially in October and November, and then severe cold and all the fluctuations for the better part of two months, which is continuing on actually. But regardless, that has just had a significant impact overall in terms of our ability to ship certainly in some cases.

Ketan Mamtora

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I see. That's helpful. And then, Alan, on the capital expenditure guidance that you gave can you highlight maybe a couple of kind of key projects that you have both in lumber and pulp? And how much of what you kind of guided to is maintenance in that both in lumber and pulp?

Don Kayne

For sure. Maybe, Alan, you could come in on that.

Alan Nicholl

Yeah. Absolutely. Good morning, Ketan. So to answer your question, the numbers that we've given you are—they got typically close to 50 percent would be for lumber anyway would be mostly maintenance or certainly sustaining projects.

A key focus for us next year in Western Canada will be drying, and so we've got a number CDKs that we're building in to our budget. In the US site, clearly we're very keen with a lot of our discretionary spend to support the significant margins that we're getting there, but optimization, some upgrades that just all of which are really aimed at driving further improvements in productivity whilst preserving our strong margins.

In terms of pulp there's some maintenance projects in there; there's a couple of energy projects we're looking at as well. And so we'll be refreshing our analysis regularly as we go through the year.

But hopefully that gives you a flavour of some of the thinking that's embedded in our numbers.

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**Ketan Mamtora**

No, sure it does. That's helpful. And just one follow-up on that; how much of these kind of projects help you to increase capacity in the US South? Or these are more kind of productivity cost-reduction kind of projects?

Don Kayne

I think it's probably a bit of both. And I think that I believe we talked last time around that we thought it would be in the neighbourhood of between 100 million and 200 million board feet positive impact through the capital that we're spending and on both the revenue opportunity, but as well as the cost-reduction opportunities.

Ketan Mamtora

I see. That's helpful. And then last question, just kind of talk us through how you are thinking about kind of capital allocation, M&A; obviously balance sheet is in a pretty good shape both over at Canfor Corp. and on the pulp side, and especially considering this whole uncertainty around kind of the lumber trade dispute how you are thinking about your drive to increase capacity in US South?

Don Kayne

Yeah. I think, Ketan, I'll let Alan talk about the pulp side particularly around the buybacks. But as we've indicated at several of these analyst calls over the last probably several years, our capital allocation continues to be focusing on the balance sheet and reducing debt. We would certainly,

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though, we've felt particularly in the last year, 18 months, we've made significant progress around that in terms of our debt reduction.

Certainly after that capitalizing the facilities we've continued to do that, as you spoke about. We'll continue to do that going forward in both the north and the south; still some opportunities there. And then, of course, the buybacks what Alan will talk about and then, of course, M&A. And as a result of the debt reductions that we've made the last 12 to 18 months, we'll continue like we have been is looking at some of the opportunities that no doubt will present themselves. Notwithstanding, valuations will continue to be an issue here perhaps, but that's where it stands.

Alan, why don't you maybe talk to Ketan a bit about our pulp side around buybacks and our stance on that?

Alan Nicholl

Yeah. Yeah. No. For sure. Thanks, Don. So I think we've guided in recent quarters around the fact that we've been taking what we call the pause from share buyback behaviour. I think that was largely predicated on some of the pressures that we saw coming in on the supply side.

We're certainly encouraged by what we're seeing on the pricing front, and our outlook for this year is much better than it was even six months ago. So with a stronger balance sheet and a stronger outlook for this year, I think we're keen clearly to support not just significant capital effort, but keen with the board's strong support to renew our share buyback activity here as we go through 2017.

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**Ketan Mamtora**

Okay. That's very helpful. Appreciate all the colour, and good luck in 2017.

Alan Nicholl

Thanks, Ketan.

Operator

Thank you. Your next question comes from Sean Steuart from TD Securities. Please go ahead.

Sean Steuart — TD Securities

Thanks. Good morning, everyone.

Don Kayne

Good morning, Sean.

Sean Steuart

Question on the current surge we're seeing in Western SPF pricing. How much of that would you attribute to shipment management around the potential for critical circumstance assessment? And, Don, I gather by your comments before you guys haven't curtailed any volume based on that potential assessment. Is that correct?

Don Kayne

Yeah. Well, I'll let Wayne talk about some of the detail there, but yeah, absolutely. I mean we've said all along—and I know you know this, Sean, probably—is that we've been supportive of

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diversification from the start and then the importance of overseas shipments. And so really ourselves we've continued on that path, and we think it's the right one clearly. And as a result of that, we're confident that we'll be under the threshold for critical circumstances.

But, Wayne, you've been doing a lot of work on that so why don't you fill Sean in on a few of those things?

Wayne Guthrie — Senior Vice President of Lumber Sales and Marketing, Canfor Corporation

Sure. Thanks, Don. From our perspective, Sean, there's a few things happening here. First of all, the market in the US is very good. Customers are needing more lumber. The demand—the order files coming in, their orders are coming a little bit faster than they anticipated. And I think they're a little bit shorter of inventory than they thought they were going into 2017. So good underlying demand even before we get into all the noise around the trade file.

Secondly, we're seeing and you saw at the end of last year you saw five consecutive months of increased shipments to China. You've heard all about low inventories over there, which we can validate are still the case. And so you've got more draw from China than, quite frankly, anybody anticipated, and we expect that going right through 2017. So that's the second thing.

And then you add the emotion and the confusion and the reality that some of the players have reduced shipments. So you add all that up and it's created this bit of a storm here that we're seeing on pricing right now.

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It all has—as Don talked about in his opening comments, you've got to be—there's a lot of emotion right now about that topic, but we're going to stick with the plan. We've got markets all around the world. We'll just continue to stay disciplined and focused on our customers, but I think that this volatile price environment is likely here to stay for a while as we get through the next few quarters.

Sean Steuart

And, Wayne, just one follow-up on China; you mentioned better volumes through the latter part of 2016, but it looked to me like the December volumes pulled back quite a bit. Was that—you mentioned for your business on pulp there were vessel delays tied to weather. Did the weather affect any of the volumes to China in December? And I gather you're seeing better volumes to start the year?

Wayne Guthrie

Yeah. So good catch; December was down a little bit. But like what happened in our pulp business, we had several vessels delayed. There's actually congestion here at the Port of Vancouver, and so we've got some late shipments into that market.

You've also got the complication of Chinese New Year, which kind of messes up shipments. I think the absolute number in January when we get the reports out it'll be down as well, but our order book has been consistently increasing; not dramatically, but consistently increasing. And once

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we get through the noise of the congestion, once we get through Chinese New Year I think we'll see that trend continue.

I think you'll see some shippers have to go back to Prince Rupert to alleviate some of this congestion down here, and we're working on some of those things to—because the demand looks pretty solid going into Asia.

Sean Steuart

Great. Thanks for the context, guys. That's all I had.

Don Kayne

Thanks, Sean.

Operator

Thank you. Your next question comes from Paul Quinn from RBC Capital Markets. Please go ahead.

Paul Quinn — RBC Capital Markets

Yeah. Thanks. Good morning, Don and Al.

Don Kayne

Good morning, Paul. How are you?

Paul Quinn

Good. Just a question on—or a clarification on softwood lumber negotiations. Are you referring to company-to-company negotiations? Because my understanding was Trump

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administration wasn't in place yet for government-to-government stuff. And when do you expect that to happen?

Don Kayne

Yeah. More just the preliminary discussions I think more with the new groups down there, which some of them still not formed 100 percent yet. So I guess all I was really trying to indicate, I think, is that we're—there's some proactive stuff that's going on; just trying to get a handle on it.

Clearly, Paul, there'll be a huge education process necessary here because we've got the new administration, like you said. So we're not expecting any immediate answer to this deal at all. But clearly there's a lot of work that is being done and has been done that we will try to—I'm certain that the Canadian government at least will be working hard on trying to get some of the key points across, right?

So yeah, so we'll see how it goes here. But that's what I was referring to.

Paul Quinn

All right. And then just staying with the file, one of your Canadian peers suggested that they'd be okay with a quota. Are you of the same opinion or open mind on the subject of resolution?

Don Kayne

Yeah. I guess from our standpoint, clearly as we've talked before, Paul, and we would still be of the same opinion, is it's likely for us anyway going to come down to some market share number, and so that's going to be critical. And so it's the market share number.

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But there's a whole host of other factors as well as the market share on its own. And people tend to just talk about market share, but there's some other key points maybe equally important that have to be considerations as well that I wouldn't want to speak about on the phone. But certainly we're looking at it as likely to be down the road here is related probably more to market share.

Paul Quinn

Okay. And then just flipping over to, I guess, the pulp side. We're seeing some strength in short-term pricing here. How sustainable do you think that is in light of the capacity additions coming to the market later this year in 2018?

And then secondly, I'm hearing rumours of an investigation on the pulp side—potential collusion—which I suspect happens all the time in the marketplace when buyers are seeing higher prices. But have you got any knowledge of that?

Don Kayne

Maybe—thanks, Paul—I'll let Peter answer that—take that question, if that's okay.

Peter Hart — Vice President of Pulp Sales, Canfor Corporation

Okay. Thanks, Paul. Certainly as we look from now to the end of the second quarter we expect to see continued positive momentum in the pulp side, particularly because of the upcoming spring maintenance season. For the second half of the year there could potentially be some challenges as new capacity ramps up.

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As to your second comment about potential investigation, not something I've heard of at all.

Paul Quinn

All righty then. Thanks very much. Best of luck, guys.

Don Kayne

Great. Thanks, Paul.

Operator

Thank you. Your next question comes from Hamir Patel from CIBC. Please go ahead.

Hamir Patel — CIBC

Hi. Good morning.

Don Kayne

Good morning, Hamir.

Hamir Patel

Just clarify for us all, is it only the countervailing duties that are currently in that sort of potential retroactive period? Because it just seems to me like the lumber market's behaving as if the antidumping duties are also retroactive right now potentially.

Don Kayne

Yeah. What we're referring to right now is just countervail.

Hamir Patel

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Right.

Don Kayne

Which is a preliminary date for that. As you probably know, it was late April, so assuming anybody that got caught up with that it would be three months prior to that, so early February essentially, like right now. You'd be in it right now if you—potentially—if you were overshipped into the United States.

Hamir Patel

Right. And then the retroactive and the dumping would be April 1st then—

Don Kayne

Well, the preliminary determination, I believe, is April 29th to be exact. And so you'd be three months prior to that, so you're looking at whatever that is, January 29th, February 1st really.

Hamir Patel

Yeah. And on the countervailing I guess I meant for the—when we get the dumping—

Don Kayne

Oh, antidumping. Okay.

Hamir Patel

Yeah.

Don Kayne

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So the antidumping is, sorry, the end of June is when the preliminary determination is. So three months prior to that, so whatever that is; I guess that's March.

Hamir Patel

Right. Okay. That's helpful. And—

Don Kayne

As I mentioned, we're one of the respondents for both, right, so.

Hamir Patel

Right. Okay. And then I just had a question about log cost inflation. What's your expectations for this year in both the US South and BC?

Don Kayne

Why don't you, Alan, why don't you go ahead?

Alan Nicholl

Yeah. No, for sure. Good morning, Hamir. So in terms of the US South, we continue to see very muted log cost prices, so we're forecasting log costs to be fairly flat again this year.

With respect to Western SPF, we're forecasting just a couple of percent increase this year, Hamir.

Hamir Patel

Thanks for that, Alan. And just a final question I have for Wayne. You referenced— appreciate your comments on the China market and realize that things might change depending on

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how the trade case unfolds. But what's your expectation this year for volume growth on the export front?

Wayne Guthrie

Well, to your point, it really depends on how this trade thing unfolds, right, and I think a lot of guys will react to that. If you leave that aside for a second, I think you're going to see continued increased demand in China; like could be significant.

I think there's two things happening in China that we quite frankly didn't expect to get as much traction that's happening. There's a lot of wood frame housing going on, especially in higher-end resort-type developments. And that is a draw now for specifically for Canadian lumber or North American lumber. And the Europeans made huge advances in the last couple of years in the furniture sector, and that's kind of a road map for some of the higher-value products that we're producing.

So I think you will see continued growth in China maybe not on the commodity side, but just in absolute volume there'll be definite growth there.

Japan, we're really pleased at the resiliency of that market. I mean our sales were up a little bit last year—very minor, low single-digit percentages—but still up. And this year we expect at least flat, maybe up a little bit.

So Asia looks pretty stable.

Hamir Patel

Okay. Great. Thanks, Wayne. That's all I had.

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Don Kayne

Okay. Thanks, Hamir.

Operator

Thank you. Ladies and gentlemen, this concludes today's conference. We thank you for participating. You may now disconnect your lines.

Don Kayne

Thanks, Operator, and thanks, everyone, who participated. We'll talk to you at the end of the next quarter.

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