

## CORPORATE PARTICIPANTS

### **Don Kayne**

*President & Chief Executive Officer, Canfor Corporation  
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### **Alan Nicholl**

*Chief Financial Officer, Canfor Corporation & Canfor Pulp Products Inc.*

### **Alistair Cook**

*Senior Vice President, Wood Projects Operations, Canfor Corporation*

### **Wayne Guthrie**

*Senior Vice President, Sales & Marketing, Canfor Corporation*

### **Brett Robinson**

*President, Canfor Pulp*

## CONFERENCE CALL PARTICIPANTS

### **David Quezada**

*Raymond James*

### **Sean Steuart**

*TD Securities*

### **Mark Kennedy**

*CIBC World Markets*

### **Paul Quinn**

*RBC Capital Markets*

## PRESENTATION

### **Operator**

Good morning, ladies and gentlemen. Welcome to the joint Canfor Corporation and Canfor Pulp Products Incorporated Second Quarter Results 2013 Conference Call. A recording of the call and a transcript will be available on the Canfor and Canfor Pulp 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, President and CEO of Canfor Corporation and CEO of Canfor Pulp Products Inc. Please go ahead, Mr. Kayne.

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### **Don Kayne**

Good morning everyone and thanks for joining the Canfor and Canfor Pulp Second Quarter Results Conference Call. I will speak briefly to the results of both companies before I turn things over to Alan Nicholl, who is our Chief Financial Officer for both Canfor Corporation and Canfor Pulp Products Inc. Alan will provide a more detailed overview of our performance in quarter two, after which we will take questions. With me today to address your questions are Brett Robinson, President of Canfor Pulp; Alistair Cook, Senior Vice President of Wood Products Operations; Wayne Guthrie, Senior VP of Sales and Marketing for Canfor; and Sean Curran, VP of Sales and Marketing for Canfor Pulp.

So Canfor Corporation posted a quarter two net income of \$110 million, which is an improvement over the net income of \$62 million posted in quarter one. Of this \$110 million, \$7.6 million is attributable to Canfor Pulp and the balance to our solid wood business. Improvements in our results over Q1 are largely related to increased shipments of lumber and, to a lesser extent, improvements in our manufacturing cost.

As you are all well aware, we saw a significant correction in lumber prices from the eight year high they achieved in quarter one. Mostly the sliding prices is supply related, owing to increased shipments and railcar availability. We did, however, also see reduced housing activities in the United States due to unseasonably wet weather. Housing starts were down 9 percent from Q1. That being said, we feel that the underlying housing demand in the U.S. remains encouraging and that we will continue to see steady and positive trends in the U.S. housing market going forward.

Canfor announced in late May that we had reached agreement with the Scotch & Gulf Lumber Company in Alabama to acquire their facilities in Mobile, Fulton, and Jackson, Alabama over a three-year period. We expect the deal to close next month. The deal will add about 440 million board feet to our lumber capacity. Increasing our capacity in Southern Yellow Pine will improve our ability to serve our U.S. customer base.

We've seen modest improvements in pulp markets through the quarter. Canfor Pulp's shipments were steady through the quarter and in line with Q1. Results in the current quarter were impacted by the scheduled

maintenance outages at Northwood and Intercontinental pulp mills. We continue to make progress on our capital plans with projects well underway in our Elko and Mackenzie sawmills. The new continuous kiln in our Conway sawmill in South Carolina started up in June. Canfor Pulp's maintenance capital program progressed well through quarter two and we anticipate that minimal maintenance downtime through Q3 will be reflected in our results.

I'd like to now turn the call over to Alan Nicholl, who will provide more details on our financial results.

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### **Alan Nicholl**

Thank you, Don, and good morning everyone. My comments will focus principally on our financial performance for the second quarter of 2013 by reference to the previous quarter. I'll discuss the results of Canfor first and then Canfor Pulp second.

In my comments I'll be referring to our second quarter overview slide presentation, which you'll find on either the Canfor or Canfor Pulp websites in the Investor Relations section under Webcasts. Full details are contained in the Canfor and Canfor Pulp news releases, both of which were issued yesterday.

For the second quarter of 2013 Canfor reported shareholder net income of \$110 million or \$0.77 per share, well ahead of shareholder net income of \$62 million or \$0.43 per share reported for the first quarter of 2013 and \$3 million or \$0.02 a share reported for the second quarter of 2012. On slide three of our presentation we highlight various non-operating items net of tax and non-controlling interest, which affect comparability of our results between the first and second quarters. In the second quarter, the most material adjusting item was a gain of \$33 million or \$0.24 per share related to the sale of our 50 percent interest in the Peace Valley OSB joint venture. This gain is composed of net income earned in 2013 plus the estimated fair value of additional consideration that Canfor may earn over the next three years through an earn-out arrangement. The other items are largely the typical items that we adjust for each quarter. The net positive impact of these items in the second quarter was approximately \$23 million or \$0.16 a share. After taking account of the adjusted items, the second quarter adjusted net income was \$88 million or \$0.61 a share. This represented an \$18 million or \$0.12 a share improvement from adjusted net income of \$70 million or \$0.49 a share for the first quarter of 2013.

With respect to our second quarter operating performance, you'll see on slide four of our presentation

that reported operating income was \$128 million, an increase of \$28 million from the previous quarter. This increase principally reflects improved results in the lumber segment, mostly due to higher shipments and slightly lower costs. Operating results for the pulp business were steady relative to prior quarter as higher sales realizations were largely offset by costs linked to the scheduled outages at Canfor Pulp's Intercon and Northwood pulp mills in the quarter. I'll speak more on our operating performance in a few minutes when I discuss the individual segments.

Slide five shows the Western SPF benchmark lumber prices for 2x4, #2&Btr, and U.S. housing starts. U.S. lumber demand receded somewhat in the quarter as total U.S. housing starts averaged 872,000 units, a 9 percent decrease from the previous quarter. As Don previously highlighted, the decrease was principally due to a sharp drop in the more volatile multi-family starts, which were down 27 percent in June. This dip multi-family starts and, more significantly, an increase in North American production output and railcar availability accounted for sharp correction in North American lumber prices in May and June.

Turning to slide six, you'll see that the lumber segment reported operating income of a \$116 million for the second quarter of 2013, a \$27 million increase from the previous quarter. The improvement in second quarter lumber results was largely due to a 12 percent increase in shipments, reflecting both higher production and the improved railcar availability. Sales realizations were broadly in line with those for the first quarter of 2013, as a combination of stable prices in offshore markets, proportionally higher shipments in April, as well as a weaker Canadian dollar offset the impact of North American price corrections that we saw in May and June. Overall unit manufacturing costs were down slightly compared to the first quarter.

Canfor's pulp and paper segment principally comprises of the results of Canfor Pulp Products Inc. As you can see on slide seven, Canfor Pulp Products Inc. reported net income of \$8 million or \$0.11 per share in the second quarter, and this compared to net income of \$11 million or \$0.15 per share for the first quarter and net income of \$3 million or \$0.04 a share for the second quarter of 2012. Staying on slide seven, we've highlighted the common non-operating items net of tax which affect the comparability of Canfor Pulp's results between the first and second quarters. The net negative impact of these items was approximately \$8 million or \$0.11 per share in the second quarter. After taking account of these adjustments, Canfor Pulp's second quarter adjusted net income was \$15 million or \$0.22 a share and this represented of \$3 million or \$0.05 per share increase

from the \$12 million or \$0.17 a share reported for the first quarter of 2013.

The main components of Canfor Pulp's results for the second quarter are highlighted on slide eight of our presentation. Canfor Pulp's operating income was \$20 million for the second quarter, which was (substantially) the same as we reported for the previous quarter. With respect to Canfor Pulp's pulp segment, second quarter operating income was around \$15 million, the same as that reported for the previous quarter.

Global U.S. dollar NBSK pulp list prices moved up between \$22 and \$40 per tonne just depending on the region while shipments were down slightly. Pulp sales realization showed a moderate increase reflecting the higher prices as well as the weaker Canadian dollar. Unit manufacturing cost increased due to lower production and higher maintenance cost associated with the scheduled outages in the quarter. In the paper segment we reported second quarter operating earnings of \$7 million. That was up \$1 million from the previous quarter. Compared to the first quarter, higher earnings resulted from improved paper unit sales realizations and more significantly higher shipment levels.

Capital spending in the second quarter totalled \$49 million, of which \$39 million was for the lumber business and \$9 million for the Canfor Pulp. Work continued on the Mackenzie and Elko projects, both announced late last year and planed to be completed by the fall of this year. For Canfor Pulp capital spending included the previously-announced turbine projects at Northwood and Intercon. We currently anticipate that our 2013 capital spending for lumber and pulp businesses will be around \$170 million and \$50 million respectively.

Yesterday the Canfor Pulp Products Board announced a dividend payment of \$0.05 a share for the quarter, consistent with the guidance given in February of similar payments through 2013.

During the second quarter both Canfor and Canfor Pulp brought back Company shares under the existing normal course issuer bid programs. Canfor repurchased 763,000 shares at cost of \$14 million and Canfor Pulp repurchased 165,000 shares at a cost of \$1.5 million. While targeted capital spending and a strong balance sheet remain key priorities, we will continue to look for possible opportunities to repurchase additional shares for both companies over the balance of 2013.

As previously announced, on May 31 we entered into purchase agreement to buy Scotch & Gulf Lumber on a phased basis over three years. We expect, as Don mentioned, to close this acquisition of the first 25 percent

in August. The purchase price is \$80 million plus working capital.

At the end of the second quarter, Canfor, excluding Canfor Pulp, had positive net cash or \$24 million with available liquidity of \$334 million. Canfor Pulp had net debt of \$70 million with available liquidity of a \$106 million. Net debt to total capitalization excluding Canfor Pulp was negative 2 percent, for Canfor Pulp its 15 percent, and on a consolidated basis it was 3 percent.

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

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**Don Kayne**

Thanks Alan. I'd now like to open the lines up for questions.

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## QUESTION AND ANSWER SESSION

**Operator**

Thank you, Mr. Kayne. We will now take questions from the telephone lines. We will now take questions from the financial analysts. If you have a question, please press star one on your telephone keypad. If you are using a speakerphone, please lift your receiver, then press star one. If at any time you would like to cancel your question, please press the pound key. Please press star now if you have a question. There will be a brief pause while the participants register for questions. Thank you for your patience. Once again, please press star one at this time if you have a question.

Our first question is from David Quezada with Raymond James. Please go ahead.

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**David Quezada**

Thanks. Good morning, guys. Just a quick question on the cost side for lumber. It seems like the industry in general is experiencing some inflation or did relative to the first quarter anyway, whereas yours looked kind of more flat. Do you have any insight as to why that might be and maybe just discuss what the outlook is on the cost side going forward?

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**Don Kayne**

Yeah. Thanks, David. I think I'd just maybe make a brief comment on that. I mean I think that, you know, we're

working continually on our overall costs. We are seeing some of the benefits come through from our capital that we've spent over the last couple, three years, which has offset to some degree some of the log cost pressures that we're seeing. Going forward we do see, probably as others, log costs will increase somewhat here just to due to stumpage rates going up in Q3. Uncertain yet where they'll end up in Q4 but certainly on the log cost side we do see some pressure there going up. And hopefully we can balance some of that off at least on the conversion cost side.

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**David Quezada**

That's helpful, thanks. And I guess just a follow up, it seems like the price realizations you had this quarter, as was stated in the release, benefited from a lag on the offshore shipments. How do you see that dynamic playing out next quarter? How would that affect things?

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**Don Kayne**

If markets continue to move upward, as they have been here recently, hopefully there won't be much of a lag going the other way, but I do think we had some good benefit of that on Q2, as you accurately stated. In Q3, with the price drop that we've seen, there'll be some reversal of that, but we have seen it move back a little bit here in more positive territory. So hopefully that will be mitigated.

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**David Quezada**

That's great. Thank you.

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**Operator**

Thank you. The next question is from Sean Steuart with TD Securities. Please go ahead.

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**Sean Steuart**

Thanks. Good morning, everyone. A few questions. Don, I'm wondering if you can just give us an idea of, with respect to M&A opportunities, in the U.S. south I guess in particular, can you speak to other sort of Scotch & Gulf type opportunities that might be out there, and I guess, from a broader perspective, are you limiting your consideration to the U.S. south or are you broadening, I

guess, your regional set that you might look at for M&A opportunities?

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**Don Kayne**

I think Sean, just in a broad sense, I mean I think that, first of all, that the southern area or the southern region of the United States is certainly an area that we believe has got a great future, thus why we entered into the deal that we have recently with Scotch & Gulf. We think there are some good opportunities down there. How much is available and where and so forth, you know, we're working hard, as we have been, to try to make sure that whatever we do is in the strategic areas that really fit with what we have already. But certainly I would say just as a general statement that we definitely believe that's a critical region for us going forward and we'll continue to focus on it as we have. I don't know if that gives you enough information but that's kind of where we are right now. So it's a key area for us and we'll continue to look for opportunities.

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**Sean Steuart**

Okay. The sequential lumber volume pickup you saw this quarter, I guess the MD&A suggested that some of it was extra shifts, and I'm wondering if you could just quantify how much that contributed to the volume pick up this quarter and, you know, presumably down at these levels you're not running those extra shifts now, so I'm just trying to gauge I guess how much that might have benefited Q2 volumes and how much give back you might see this quarter

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**Don Kayne**

I wouldn't expect that we'd see much of a change at all. I mean where we are probably—some of the increase that we saw in Q2 was also, you know, as capital programs that we've spent and the mills get operating and progressing there, we are some benefit from that obviously from all the capital. In addition to that there has been some extra shifting as a result of that. But where we're at today we'll probably see I would say probably quarter over quarter pretty flat actually and not a lot of significant difference there, and we're kind of comfortable with where we are today.

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**Sean Steuart**

Okay. And then last question, Don, just wondering if you can give us an update of where things stand with labour negotiations.

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**Don Kayne**

For sure. Well, as you know, I'm sure that they expired June 30th with the steelworkers and we've had numerous conversations, our bargaining group has had with the steelworkers has been going, ah, it has been going well, made some good progress on several of the issues, and we still have a few more to iron out yet, and so I would expect that we will continue to make solid progress through August and hopefully we will be able to tell you a positive result here in August.

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**Sean Steuart**

That's all I had. Thanks, guys. Appreciate it.

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**Operator**

Thank you. The next question is from Mark Kennedy with CIBC World Markets. Please go ahead.

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**Mark Kennedy**

Good morning and good Q2, guys. First question, just again on fibre cost here going into Q3, we've heard numbers like in BC stumpage rates could be going up sort of \$5 to \$7 cubic meter in Q3. Would you agree with that kind of range for yourself?

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**Don Kayne**

Hi, Mark. Yes, we would.

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**Mark Kennedy**

Okay. And again, you know, depending on how I guess the market place component of that works out you may see some of that actually come off again in Q4 I guess, right?

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**Don Kayne**

That's correct. If prices were to stay where they were, we would expect that.

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**Mark Kennedy**

Okay. And then just in terms of your overall sort of CapEx profile, do you, you know, I know it's probably early, you probably haven't done your detailed 2014, but do you sort of envisage sort of 2014 CapEx levels being consistent with 2013 or is there any reason they would step up?

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**Don Kayne**

They'll be at least where they are at 2013.

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**Mark Kennedy**

Okay, but any magnitude for a significant increase on something?

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**Don Kayne**

Not necessarily. I think, Mark, just be very similar to what it is in 2013, subject to some maybe additional capital that we are looking at for some high-return projects to be determined yet. But certainly I would say that the 2013 number would be a minimum.

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**Mark Kennedy**

Okay. And would that sort of be similar for Canfor Pulp too, that its number would sort of stay in that \$50 million range next year as well?

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**Don Kayne**

Yes, that would be accurate.

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**Mark Kennedy**

Okay. All right. And then, finally, you know, obviously you will see some pressures here in Q3 with fibre, but just trying to get a sense for how much further sort of manufacturing, productivity or what else could help offset that fibre cost from productivity pickups. Is there still more sort of cost improvement coming from the productivity side in Q3 do you think?

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**Don Kayne**

For sure. I mean our focus continues to be, and it's really the fundamental reason why we have invested so heavily the last several years as we have, is to get our costs at top quartile and, as you know I think, Mark, as we've announced and are spending another \$40 million at Elko and another \$40 million Mackenzie, and also looking at probably Houston as well. So that will further improve our operating cost overall as a company. And so, yeah, over the next six to twelve months we would expect ongoing improvements.

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**Mark Kennedy**

Okay. And then finally, just comments in terms of what your big buyers in the U.S. market are saying right now as they sort of look into the back half of 2013 and into 2014, because certainly there has been some concern with the bump in mortgage rates and the weaker housing starts numbers we saw for June, there are some pessimists out there that are saying, you know, the cycle is slowing, but I am not really convinced that's the case.

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**Don Kayne**

Mark, on that one I'll let—Alistair and Wayne have been out travelling in the U.S. here recently so I'll let Wayne answer that one.

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**Wayne Guthrie**

Thanks, Don.

Our U.S customers generally are cautiously optimistic. And I know that's bit of an overused term but I think going into Q1 they were enjoying a nice uptick in businesses. It did definitely slow down in Q2. When they look at the back half of the year and into 2014 they do expect better activity, they do expect increased sales, but the well-documented issues of affordability, labour shortages, and the lack of developed land will continue to be headwinds here as we go through 2014. So it will probably grind higher but lots of headwinds out there still.

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**Mark Kennedy**

Okay. That's great, Wayne. That's it for me. Thanks.

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**Operator**

Thank you. The next question is from Paul Quinn with RBC Capital Markets. Please go ahead.

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**Paul Quinn**

Yeah, thanks very much. Just wanted to build on, I guess, the previous question on cost inflation, especially in the log side. I guess you're in agreement with that \$5 to \$7 increase in BC stumpage that we are seeing in July but what are you experiencing in terms of cost inflation on the logs that you're purchasing outside of your tenures?

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**Don Kayne**

I would say on that probably a similar number. I mean we don't look at it as closely here but for the most part we'd probably in the ballpark, very similar. Maybe even on the lower end of the \$5 to \$7.

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**Paul Quinn**

Okay. And then how would you quantify what you are experiencing at your mill in Alberta? Is that going up like a half or a quarter of what you are seeing the price increase in BC?

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**Don Kayne**

Maybe, Alistair, you can...

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**Alistair Cook**

In Alberta obviously we are going to see actual decrease here in quarter three on a stumpage basis.

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**Paul Quinn**

Okay. And then just, I guess, rounded out in the U.S. south, costs there on the log side for you were pretty flat in the quarter. What is the expectation going forward?

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**Don Kayne**

No change there at all, Paul. It has been flat, like you said or mentioned, and we don't expect any change there going forward.

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**Paul Quinn**

When do you expect a change in the U.S south? Is that a 2014 event or is that a 2015?

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**Don Kayne**

I think it's out a ways, right? It could be another 12 to 18 months out. You know, there is going to be a little pressure here and there but overall we think we can keep it relatively flat.

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**Paul Quinn**

Okay. And then just moving over to China, just if you could give us some colour on what you are seeing in that market, whether you're seeing growth in shipment volumes or whether you expect growth in shipment volumes in 2013 over 2012 and what do you expect for the back of the year?

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**Don Kayne**

On that one, Paul, we just—it's been flat, you know, the last quarter over quarter we haven't seen any decrease and going forward, as we have been continually, we believe offshore markets are going to provide us with a continued diversification opportunity and a strategic advantage. So we, you know, as we have been doing for several years, we're consistent in our belief on the Asian markets. And how much it's going to increase, hard to say, but it will be probably relatively flat for the balance of this year, which will still be a fairly big increase from last year.

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**Paul Quinn**

Okay. And then if you could just round out the, ah, I guess the pulp maintenance schedule for the balance of the year?

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**Don Kayne**

Brett, I'll let you do that one.

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**Brett Robinson**

Thank you. So, for the balance of the year we've got the PG shut in the fourth quarter and it's mini-major so it will be six days. Relatively small compared to the shuts we've already completed.

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**Paul Quinn**

Great. That's all I had. Thanks, guys.

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**Operator**

Thank you. Once again, please press star one at this time if you have a question.

There are no further questions registered at this time. I would like to turn the meeting back over to you, Mr. Kayne.

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**Don Kayne**

All right, thanks, operator, and thanks everyone who participated this morning, and we'll look forward to talking to you at the end of Q3. Thanks very much.

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**Operator**

Thank you. The conference has now ended. Please disconnect your lines at this time. We thank you for your participation.

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