

## **FINAL TRANSCRIPT**

**Canfor Corporation**

**Fourth Quarter Analysts' Call**

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**PRESENTATION****Operator**

Good morning, ladies and gentlemen, and welcome to the Canfor and Canfor Pulp Fourth Quarter Analysts' Call.

A recording and transcript of this call will be available on [canfor.com](http://canfor.com). During the 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 the 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 now would like to turn the meeting over to Mr. Don Kayne, Canfor and Canfor Pulp's Chief Executive Officer. Please go ahead, sir.

**Don Kayne — President and Chief Executive Officer, Canfor Corporation**

Thank you, Operator, and good morning, and thank you for joining the Canfor and Canfor Pulp Q4 2015 results conference call this morning.

I'll make a few brief opening comments about the quarter, 2015 overall, and our current outlook before I turn things over to Alan Nicholl, our Chief Financial Officer for both Canfor Corporation and Canfor Pulp Products Incorporated. Alan will provide a more detailed overview of our performance in Q4, after which we will take questions.

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In addition to Alan, with me today are Brett Robinson, President of Canfor Pulp; Peter Hart, our Vice President of Pulp Sales; Wayne Guthrie, our Senior Vice President of Lumber Sales and Marketing; and Stephen Mackie, Senior Vice President of Operations for Canada.

Canfor Pulp had another strong quarter, increasing its production compared to Q3 despite a major maintenance shut at our Northwood Mill. In addition, our two energy projects are fully operational, operating at designed levels, and generating the margins that were projected. Markets for pulp were steady in the quarter as the Company realized the benefit of higher shipments and relatively consistent revenue on a Canadian dollar basis as compared to Q3.

Approximately 85 percent of our pulp production being in higher-grade, premium reinforcing pulp, we continue to see good demand. Looking ahead, we see some positive momentum into the second quarter as a result of the traditional spring maintenance season. Overall, we expect our low cost structure and high value focus will continue to benefit the Company.

Turning to the lumber side of our business, Canfor grew significantly in 2015. During the year, we completed the acquisition of approximately 500 million boardfeet of Southern Yellow Pine lumber capacity, which will be fully recognized in 2016 and early 2017. Our focus continues to be on acquiring high quality mill assets located in strong fibre regions with the capacity to produce premium, specialty, and high-value products.

While spreads widened for narrow widths during Q4, we believe that going forward spreads will return to historical norms.

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Our Canadian mills performed well in 2015 and realized solid productivity gains and cost improvements. With most of our major capital expenditures now behind us, we expect to see continued improvement in margin performance in 2016.

In the fourth quarter, we announced the acquisition of the Wynndel Sawmill in southeastern British Columbia. This purchase is consistent with our high value strategy, as the mill produces premium boards and specialty products. We expect to close that acquisition in Q2.

Looking at our markets, I'd like to make a couple of comments. In China, we've seen recent improvements following the slowdown we experienced in Q3. The inventory buildup has been reduced and shipments have returned to more normal levels. We continue to focus on moving our shipments to China up the value chain and expect another solid year in the Chinese market, with our projected shipments at historical levels.

In the U.S., we continue to see good demand. Recent business with some of our key customers reinforce our view that we will see growth of 6 to 8 percent for 2016, due mostly to the slow but steady improvements in housing demand. In addition, we are seeing solid growth in the retail sector. We believe that inventory has decreased throughout the supply chain and is more closely balanced with demand.

So with that, I'll turn the call over to Alan Nicholl to provide an overview of our financial results.

**Alan Nicholl** — Senior Vice President, Finance and Chief Financial Officer, Canfor Corporation

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Well, thank you, Don, and good morning, everyone. My comments will focus principally on our financial performance for the fourth quarter of 2015 by reference to the previous quarter, and full details of our results are contained in the Canfor Pulp and Canfor news releases, both of which were issued yesterday afternoon.

And 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 2015, Canfor reported shareholder net income of \$2 million or \$0.01 a share. That was up from a net loss of \$17 million or \$0.13 a share reported for the third quarter and down from net income of \$30 million or \$0.22 a share reported for the fourth quarter of 2014.

On Slide 3 of our presentation, we highlight various non-operating items, net of tax and non-controlling interests, which affect the comparability of our results between the respective quarters. After taking account of these adjustments, the fourth quarter adjusted shareholder net income was \$8 million or \$0.06 a share, compared to similarly adjusted net income of \$6 million or \$0.05 a share for the third quarter.

As set out on Slide 4 of our presentation, Canfor's fourth quarter operating income was \$32 million, an increase of 23 million from the previous quarter. After adjusting for onetime costs, most

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notably the \$19 million Canal Flats Sawmill closure provision that we recorded in the previous quarter, operating income was up \$7 million compared to the third quarter.

Results for the Lumber segment are highlighted on Slide 5 of our presentation. After adjusting for the aforementioned onetime items and a favourable inventory valuation adjustment of \$6 million in the current quarter, the Lumber segment reported a small operating income of \$1 million; that was up \$2 million from the \$1 million loss reported for the previous quarter. The increase principally reflected higher Southern Yellow Pine sales realizations, improved productivity at the Western Canadian SPF's operations, as well as the incremental contribution of the newly acquired Anthony Forest Products operations for the last two months of the year.

Total lumber production was up by 6 percent from the previous quarter, reflecting higher operating rates, particularly in the western Canadian operations, as well as the addition of Anthony's, which more than offset the impact of the Canal Flats Sawmill closure.

Overall, unit manufacturing costs were in line with the previous quarter, reflecting the improved productivity, which offset seasonally higher energy costs. Lumber shipments were relatively flat compared to the third quarter but were up 24 percent compared to the same quarter of 2014, reflecting our expanded presence in the US South.

Canfor's Pulp and Paper segment comprises the results of Canfor Pulp Products Inc., and as you'll see on Slide 6 of our presentation, Canfor Pulp reported net income of \$30 million or \$0.43 a

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share compared to net income of \$31 million or \$0.45 a share for the third quarter and net income of \$21 million or \$0.29 a share for the fourth quarter of 2014.

Canfor Pulp's fourth quarter adjusted net income was \$29 million or \$0.42 a share, and this represented a \$6 million or \$0.08 a share decrease from adjusted net income of \$35 million or \$0.50 a share for the previous quarter.

Canfor Pulp's results, as highlighted on Slide 7, reflected US dollar NBSK list prices, mitigated somewhat by the 2 percent weaker Canadian dollar. Unit manufacturing costs were slightly higher than the previous quarter, mostly due to planned costs associated with the scheduled maintenance outage taken at the Northwood pulp mill, which more than offset higher operating rates.

Pulp production was up 4 percent from the third quarter and the results also included seasonally higher energy prices, which boosted our energy revenue in the quarter.

Results in the Paper segment were down slightly, reflecting lower prices and proportionately lower shipments to North America, partly offset by the weaker Canadian dollar.

Capital spending in the fourth quarter totalled \$84 million, of which 54 million was in the lumber business and \$28 million in Canfor Pulp. In total, 2015's capital spending was \$172 million for Canfor and \$68 million for Canfor Pulp. And looking out to 2016, we currently anticipate capital spending of around \$155 million for our lumber operations and \$75 million for Canfor Pulp.

For the fourth quarter, Canfor Pulp's Board of Directors approved a quarterly dividend of \$0.0625 a share. And also during the fourth quarter, Canfor repurchased approximately just over 1

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million shares at an average price of \$19.05, while Canfor Pulp repurchased just under 700,000 of its common shares at an average price of \$14 a share.

At the end of 2015, Canfor, excluding Canfor Pulp, had net debt of \$484 million with available liquidity of 192 million. Canfor Pulp had net debt of \$33 million with available liquidity of \$117 million.

Net debt to total capitalization, excluding Canfor Pulp, was 26 percent; for Canfor Pulp it was 6 percent, and on a consolidated basis, it was 24 percent.

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

**Don Kayne**

Thanks, Alan. And so, Operator, we'll take questions.

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## 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 \*, followed by 2. Please press \*, 1 now if you have a question. There will be a brief pause while participants register for the questions. We appreciate your patience.

And your first question will be from Sean Steuart at TD Securities. Please go ahead.

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**Sean Steuart** — TD Securities

Thanks. Good morning, everyone. A few questions: Alan or Don, the 155 million you have budgeted for CapEx at the sawmills this year; I gather the bias is to the US. Can you give us a sense of, maybe in percentage terms, how much of the total CapEx is going to the US South? And then what percent going to the US is for kilns versus other discretionary CapEx initiatives there?

**Don Kayne**

Sure, Sean. It's Don. Maybe what I'll do, Alan, you maybe can...

**Alan Nicholl**

Yeah. I'll start it off. Yeah, Sean, so you're right. We're targeted around 155 million for lumber business. That's kind of in line with the depreciation that we're anticipating for the year. I would say about half of it's destined to the US side and obviously the other is for the western Canadian operations.

In terms of kilns, I just don't have that in mind for you. There is some money set aside for CDKs, but the exact amount I just can't give you right now. But we'll follow up and give you that amount after the call.

**Sean Steuart**

Okay. Thanks for that. And then you mentioned, Don, the trends you've seen early in the year in lumber volumes to China. Can you speak a little bit more to the mix you have there? I know

that transitioning to a higher value mix has been a trend you've witnessed. Any context you can provide on how that's continuing to trend this year?

**Don Kayne**

Yeah. For sure, Sean. I'll let Wayne answer some of that, specifics for that, but just at the outset, just to reinforce what I said in my comments, is that we have—it's been again, another pretty decent year in China overall with the fourth quarter seeing a decent rebound and gives us more confidence going forward into 2016 to kind of end up with pretty similar levels to where we've been in the past.

And I'll let Wayne talk about it, because he is doing a lot of work on the topic you mention there, in China, which I think is also helping us, Wayne, so go ahead and provide that colour.

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

Sure. Thanks, Don. So, Sean, our mix, our low-grade percentage is probably going down a little bit in China, just as our fibre quality improves, we're making a little bit less, and we're replacing that volume with products that I think you've heard us mention before. We're trying to get into some metric-size components for the furniture industry; trying to just move up the value chain.

And in fact, that's in line with where we see a lot of our Chinese customers want to go anyway, because they're, with their labour rates and their cost of doing business, they're trying to produce higher value products. And that requires a higher value raw material. So it's in sync with where our customers want to go.

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**Sean Steuart**

Okay. Thanks for that, Wayne. And lastly, Alan, maybe you can address this. Just a question on the Canfor Pulp balance sheet; it looks like you're going to transition back to a net cash balance sooner rather than later. Any updated thoughts on returning capital to shareholders? You've been busy on the buyback and paid out a special dividend over the past year. Is the bias still on the dividend side towards special dividends, as opposed to an increase in the regular dividend? Is that the right way to think about it?

**Alan Nicholl**

I would answer it more by saying that the bias, I think, is to truly to kind of stay the course with our more of a hybrid approach, which is that lower baseline dividend of \$0.0625, complemented by share buyback. Sean, we were quite active, as you know, in the fourth quarter and quite pleased with what we got there. And we believe that that combination is still effective. It's got a lot of support from investors, and our Board's very supportive of that approach as well. So we see that as being our preferred path, at this point in time anyway.

**Sean Steuart**

Any thought potentially of a substantial issuer bid on the Canfor Pulp side?

**Alan Nicholl**

Sorry? I...

**Don Kayne**

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A substantial issuer bid on the pulp side.

**Alan Nicholl**

Yeah. So from time to time, we think through all of the areas that you would expect us to. At this point in time, we're more motivated to pursue the normal course issuer bid. We think that's working well for us, and as I say, that's our preferred path at this point in time.

**Sean Steuart**

Okay. That's all I had, guys. Thanks very much.

**Don Kayne**

All right. Thanks, Sean.

**Operator**

Thank you. And your next question will be from Ketan Mamtora at BMO. Please go ahead.

**Ketan Mamtora — BMO Capital Markets**

Yes. Thank you. Good morning, Don, Alan. Just a question on M&A. Can you talk a little bit about how you are thinking about M&A on both sides of your business, both on the pulp side as well as on the lumber side?

**Don Kayne**

Yeah, for sure, Ketan. And it's Don. Maybe I'll talk on the lumber side and maybe let Alan talk a bit on the pulp side. But just on the lumber side, I mean as you know, we've been in the M&A business here pretty good the last four, five years, strengthening our position of course down in the

South in a significant way, which we're seeing some of the benefits of that now, and then also in BC with the latest acquisition on Wynndel.

And so at this point we're really pleased with what we've done and accomplished so far from an acquisition standpoint; whether or not and to what degree do we grow even further, obviously we look at those priorities on a regular basis and try to rank them between the pulp opportunities and the lumber opportunities and the energy opportunities, frankly. And so—but what I will say is that we're very pleased with what we've done so far, and everything we do do will be based on fibre opportunities going forward. But at this point, that's about as much as I really can say overall.

Alan, is there anything you want to add on the pulp side specifically? Or Brett too, for that matter?

**Alan Nicholl**

Yeah. I think all I would say, Ketan, is that there's similar criteria that we apply to both pulp and operations for the most part. So clearly not as many high quality acquisition targets on the pulp side as there perhaps would be on the lumber side. And so it's something we keep an eye on, as you would expect, but at this point, nothing to report.

**Ketan Mamtora**

Thanks for that. That's helpful. And just two follow-up questions on that; just on the pulp side, if there were something interesting that came along, would you be willing to lever up for something like that? Or you want to maintain a more conservative balance sheet at this point?

**Don Kayne**

Ketan, I mean just as Alan articulated, I think we're looking at opportunities as they arise, and so it would depend significantly on just what the opportunity was and how it ranked within the way we prioritize our capital going forward. So I guess that's about all I could really say around that. It's certainly a consideration among many other things, right?

**Ketan Mamtora**

Right.

**Don Kayne**

So at this point, we're pretty happy where we are though.

**Ketan Mamtora**

Okay. That's helpful. And just one more follow-up on the lumber side of the business; would you have sort of a preference in terms of acquisitions between US South, BC, Alberta? Or it would depend on the opportunity that came along?

**Don Kayne**

Yeah. Again, one of our largest areas that we consider a lot is just the fibre situation in wherever we go. And so really, whether it's Alberta, whether it's BC, or whether it's Southern Yellow

Pine, at this point, we'd have to understand what the opportunity was and rank it based on that, with probably fibre being number one and there's a few other areas we would also consider.

But clearly, the South has been a key priority for us as you know going forward, and we believe very strongly in that area. At the same time, we also feel very, very strong about BC and the future here too. So I'm not sure if that really helps you too much, but that's how we're looking at it today.

**Ketan Mamtora**

That's helpful. And just one last one; are you seeing any evidence of increased offshore lumber imports into North America?

**Don Kayne**

Maybe, Wayne, you can answer that one.

**Wayne Guthrie**

On the board side of the business, there's been some; on the dimensional lumber side, it's still relatively small.

**Ketan Mamtora**

And on the board side, where really are you seeing increased imports?

**Wayne Guthrie**

Yeah. It's European board position in the US South that's been there for a while, and we expect that to stay. So on the one-inch boards, Europe plays a big role in that.

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**Ketan Mamtora**

Gotcha. That's very helpful. I'll turn it over. Good luck in 2016.

**Don Kayne**

Thanks very much.

**Wayne Guthrie**

Thank you.

**Don Kayne**

Appreciate it.

**Operator**

Thank you. Your next question will be from Paul Quinn at RBC. Please go ahead.

**Paul Quinn — RBC**

Yeah. Thanks very much, and good morning, gentlemen. Just a couple of easy questions: One; one of you highlighted the growth in Canfor's lumber platform. Just if you could outline, especially in the US South, the shift of product mix. And you also mentioned that you expect the spread to return, the historic spread between narrows and wides to return. What gives you the confidence there?

**Don Kayne**

Yeah. I'll let—on the second easy question, I'll let Wayne answer. Just on the first one, in terms of our growth down there, are you just more interested in the scale of the growth and more

around the product mix within that scale? I mean I think, just on that, I think, overall we'll see our business, Paul, has gone from, I don't know, 10, 12 percent two, three years ago, will be, at the end of this year, close to 25 percent. And our plan is to take that up to 30 percent or maybe even higher, but certainly 30 percent will be a good number.

But as equally important in that, as we've spoke about I think a little bit before, is the makeup of that 30 percent. And the real focus through our choices of purchasing areas with real high fibre regions, is really on the premium products, right, and the high-value products. And that's really what we're focusing on within that 30 percent going forward; so less on the commodity; more on the specialties; really differentiating ourselves as much as we can from others.

### **Wayne Guthrie**

It's Wayne. Maybe on the spread question, I mean, in our models we've just learned over the years that this industry has a—history has a tendency to repeat itself. So when we're looking out and trying to project the future here, we tend to go back to 5- and 10-year averages to kind of guide us into the future.

Secondly, and more specifically, the Yellow Pine; we do expect Yellow Pine to kind of creep up in production over the next several years and SPF may well be either flat, maybe even down a touch. If that happens, the premium that we're seeing today may well start to go back to where it's been.

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As Don alludes to though, we don't spend a lot of time worrying about the price of one width versus another. Our business down there is really, really focused on specialty products, on MSR's, on lamstocks, on board, on things that we can kind of differentiate ourselves from the competition and quite frankly, from the print.

**Paul Quinn**

Okay. Then how would you describe your level of flexibility? So say, for example, 2x4s, prices start to track up off 2x8, 2x10, which was what we've seen. Are you able to flex that way? And are you comfortable with your degree of flexibility? Is that something that you're trying to increase going forward?

**Don Kayne**

Wayne, you've been down there a lot lately, so why don't you comment on that because you'd have the real good knowledge on that.

**Wayne Guthrie**

I'd say it's pretty good, Paul. I think we spent the money on that in the last little while. We're not maybe where we need to be in all operations for sure, but some of the newer acquisitions, particularly on central and west side, have a tremendous amount of flexibility. So that's kind of the model that we want to move some of the other operations towards.

**Don Kayne**

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One thing maybe just to add to that, Wayne, too, is the log size that we have down there; because the log size and quality both are quite large down there, clearly you've got a lot more opportunity to be flexible when you've got a big log as opposed to a small log. And so most of the mills that we have down in the South, I think, Wayne, for the most part, are pretty big.

**Wayne Guthrie**

For sure on the west side, that is absolutely true.

**Don Kayne**

Right.

**Paul Quinn**

Okay. Then just switching over to the softwood lumber file. I understand in March we have a meeting between Trudeau and Obama. Is it safe to say that that kicks off negotiations between the two sides? And the second part was really, just wondering if your ownership in the US South has changed any of the conversations among US South sawmillers?

**Don Kayne**

The second question first is no. That's the simple one. We haven't seen any—I mean, they're aware of it. I guess maybe from the standpoint that we certainly are much more in tune with the operating conditions down there and the operational metrics, they know that we understand that a lot better than we did maybe back in 2006.

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But aside from that, we're aware, of course, of the Obama/Trudeau meeting coming up here. But I think for now what we understand is is there's negotiations—or not negotiations so much as discussions really going on between the two governments and ourselves. Not much to really comment over and above that at this point. We'll just have to see what happens here, but there's a lot of work that has to be done here over the next little while to make progress. So time will tell here what happens as a result of that.

**Paul Quinn**

Okay. Last easy question; just on the pulp and paper side, the 75 million in CapEx. What are you spending that on?

**Don Kayne**

Maybe Brett—Brett, can you hear us here?

**Brett Robinson** — President, Canfor Pulp Products Incorporated, Canfor Corporation

Yeah, absolutely.

**Don Kayne**

Maybe you could comment on that then and give Paul some colour on that one?

**Brett Robinson**

So on the pulp and paper side, we've really changed our focus over to cost reduction; things like O2 delay, wash press upgrades, anything that can drive costs down and protect our position.

**Paul Quinn**

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Okay. So that 75, what would that break into sort of maintenance and then strategic capital?

Is that like a 40/35 split?

**Alan Nicholl**

Sorry, Brett. I'll just answer here. I think you're pretty close with that, Paul.

**Paul Quinn**

Wow, got lucky. Okay. Best of luck, guys. Thanks.

**Don Kayne**

Everybody does once in a while. That's good.

**Operator**

Thank you. Your next question will be from Hamir Patel at CIBC Capital Markets. Please go ahead.

**Hamir Patel — CIBC Capital Markets**

Hi. Good morning. Wayne, first question for you on the lumber exports to the China side. It looks like your guys' volumes were, by my calculations, up maybe 2, 3 percent in '15. We know the industry was down about 13 percent and some of your peers were down in the 30 percent range. What do you think drove that difference?

**Wayne Guthrie**

I think that about the middle part of last year, going into Q3 there, shipments from Canada dropped and bottomed out in August/September. And that was a combination of pushback from

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China and also better pricing in the US and some exchange gains and what not. So it was a short-term gain to maybe switch some volume over to the US.

What ended up happening very quickly, though, was the inventory got addressed, the inventory overage in China got addressed very quickly, and by the mid-part of Q4, there was some attractive pricing and attractive volume back in China again. So by being stable there and by being loyal and having really good customers, we were able to pick up some late Q4 business that was quite attractive to us. So I think that was a differentiator.

The bigger issue maybe is just that product mix that I alluded to earlier on the call where really it was a low-grade problem. So that was the issue in China. Our high-grade business didn't really see any dip in volume at all.

**Hamir Patel**

Okay. Thanks. That's helpful. And just a final question I had on the pulp side of the business. You guys reported energy revenues were up about 25 percent last year. I know this year you should have all three turbines running for the full year. What's the sort of dollar figure savings you're anticipating for '16?

**Alan Nicholl**

Yeah. So Hamir, it's similar to what we've disclosed previously, that we're getting close to this annualized run rate number of 25 million EBITDA, annualized.

**Hamir Patel**

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

**Operator**

Thank you. At this time, Mr. Kayne, we have no other questions registered, so I would like to turn the meeting back over to you.

**Don Kayne**

All right. Thank you, Operator, and thanks, everyone, for joining the call and your interest in Canfor, and we look forward to talking to you at the end of the next quarter. Thank you.

**Operator**

Thank you, sir. Ladies and gentlemen, this does indeed conclude your conference call for today. Once again, we thank you for participating and ask that you please disconnect your lines. Have yourselves a great day.

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