

February 8, 2011

## **CANFOR PULP PRODUCTS INC. ANNOUNCES FOURTH QUARTER 2010 RESULTS**

Vancouver, BC – Canfor Pulp Products Inc. (CPPI) (TSX: CFX) today announced Canfor Pulp Income Fund (the Fund) fourth quarter 2010 results as well as the results of Canfor Pulp Limited Partnership (the Partnership) in which CPPI has a 49.8% ownership.

On January 1, 2011 the Fund was converted to Canfor Pulp Products Inc., a taxable Canadian corporation.

The Partnership reported record sales of \$266.1 million and net income of \$47.9 million, or \$0.68 per unit, for the quarter ended December 31, 2010. The Partnership generated EBITDA of \$58.6 million in the quarter. The Fund reported net income of \$23.9 million, representing the Fund's share of the Partnership's net income and a future income tax recovery of \$0.1 million.

In the quarter, the Partnership generated adjusted distributable cash of \$48.3 million, or \$0.68 per unit, and the Partnership and the Fund declared distributions of \$1.05 per unit.

For the year ended December 31, 2010, the Partnership reported record revenue of \$1.0 billion and generated net income of \$178.0 million, EBITDA of \$230.0 million and adjusted distributable cash of \$207.1 million, or \$2.91 per unit. Cash distributions declared during the year by the Partnership and Fund totaled \$2.58 per Partnership and Fund unit.

Partnership results for the quarter were supported by increased shipment volumes, offsetting some of the impact of slightly lower prices and seasonally higher production costs. The scheduled maintenance outage at the Northwood Pulp Mill was extended for additional work on the recovery boilers and completed in the fourth quarter reducing production by 6,000 tonnes in the quarter.

Modest downward pressure was exerted on pricing in the latter half of 2010 with the restarts of the majority of Chilean pulp mills after the earthquake and two idled NBSK North American pulp mills. However, strong global softwood demand in the fourth quarter, led by China, maintained world producer and customer inventories at low levels. North American NBSK pulp list prices closed 2010 at US\$960 per tonne representing a US\$30 per tonne decrease from September 2010, but an increase of US\$110 per tonne or 13% when compared to the closing price in 2009.

Current demand remains solid with continued strong shipments into China and sustained demand in European and North America Printing and Writing paper sectors. The global softwood pulp market is expected to remain balanced through the first quarter of 2011 with the demand and supply levels expected to support current pricing.

The first quarterly dividend of CPPI is expected to be declared on or about April 30, 2011, concurrent with the release of the first quarter 2011 results. As contemplated in the Fund's information circular dated March 16, 2010 (the "Circular"), the directors intend to designate such dividends as "eligible dividends" to provide eligible shareholders with the enhanced gross-up and dividend tax credit mechanism under the Canadian Income Tax Act.

### **Additional Information**

A conference call to discuss the fourth quarter 2010 financial and operating results will be held on Wednesday, February 9, 2011 at 8:00 a.m. Pacific time.

To participate in the call, please dial 416-340-2216 or Toll-Free 1-877-440-9795. For instant replay access, please dial 905-694-9451 or Toll-Free 1-800-408-3053 and enter participant pass code 1356351. The conference call will be webcast live and will be available at [www.canforpulp.com/investors/webcasts.asp](http://www.canforpulp.com/investors/webcasts.asp).

This news release is available on the Partnership's website at [www.canforpulp.com](http://www.canforpulp.com).

## About Canfor Pulp Income Fund

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

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## Forward-Looking Statements

*Certain statements in this press release constitute "forward-looking statements" which involve known and unknown risks, uncertainties and other factors that may cause actual results to be materially different from any future results, performance or achievements expressed or implied by such statements. Words such as "expects", "anticipates", "intends", "plans", "will", "believes", "seeks", "estimates", "should", "may", "could" and variations of such words and similar expressions are intended to identify such forward-looking statements. In some instances, material assumptions are disclosed elsewhere in this press release in respect of forward-looking statements. Other risks and uncertainties are detailed from time to time in reports filed by the Fund and/or CPPI with the securities regulatory authorities in all of the provinces and territories of Canada to which recipients of this press release are referred for additional information concerning the Fund, CPPI and the Partnership, their prospects and uncertainties relating to the Fund, CPPI and the Partnership. Although we believe that the expectations reflected by the forward-looking statements presented in this press release are reasonable, these forward-looking statements are based on management's current expectations and beliefs and actual events or results may differ materially. New risk factors may arise from time to time and it is not possible for management to predict all of those risk factors or the extent to which any factor or combination of factors may cause actual events and results, performance and achievements of the Fund, CPPI and the Partnership to be materially different from those contained in forward-looking statements. The forward-looking statements speak only as of the date on which such statement is made, are based on current information and expectations and the Fund, CPPI and the Partnership assume no obligation to update such information to reflect later events or developments, except as required by law.*

*Forward-looking statements in this press release include statements made under:*

- "Critical Accounting Estimates" on page 4;
- "Income Trust Conversion Rules" on page 5;
- "Conversion to International Financial Reporting Standards" on page 5;
- "Outlook – Pulp" on page 11;
- "Outlook – Kraft Paper" on page 13;
- "Financial Requirements and Liquidity" on pages 14 and 15;
- "Critical Accounting Estimates" on page 16;
- "Conversion to International Financial Reporting Standards" on pages 16 – 19;
- "Distributable Cash and Cash Distributions" on pages 20 and 21.

*Material risk factors that could cause actual results to differ materially from the forward-looking statements contained in this press release include: general economic, market and business conditions; product selling prices; raw material and operating costs; exchange rates; changes in law and public policy; and opportunities available to or pursued by the Fund and the Partnership. Additional information concerning these and other factors can be found in the Fund's Annual Information Form dated February 18, 2010, which is available on [www.sedar.com](http://www.sedar.com).*

## Canfor Pulp Income Fund and Canfor Pulp Limited Partnership Fourth quarter 2010

The information in this report is as at February 8, 2011.

### CANFOR PULP INCOME FUND

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

The Fund was converted into a dividend paying public taxable Canadian corporation named Canfor Pulp Products Inc. (CPPI), on January 1, 2011 under the previously announced plan of arrangement approved by unitholders in April 2010. Under the arrangement, unitholders of the Fund received, for each unit of the Fund held, one common share of CPPI. The reorganization was completed with the winding up of the Fund and Trust.

At February 8, 2011, there were a total of 35,493,505 CPPI shares issued and outstanding, and CPPI indirectly held a total of 35,493,542 units of the Partnership, representing 49.8% of the Partnership. Canadian Forest Products Ltd. (Canfor) held 35,776,483 Class B Exchangeable Limited Partnership Units, representing 50.2% of the Partnership. The Class B Exchangeable Limited Partnership Units are indirectly exchangeable for an equivalent number of CPPI shares pursuant to the terms of an amended exchange agreement (Exchange Agreement) dated January 1, 2011 among Canfor, CPPI, the Partnership and the General Partner. The Exchange Agreement contains, among other things, the procedure through which the Class B Exchangeable Limited Partnership Units may be exchanged for CPPI shares.

Prior to the January 1, 2011 conversion, each unitholder participated pro-rata in any distributions from the Fund. Under income tax legislation, income tax obligations related to the distributions of the Fund were the obligations of the unitholders and the Fund was only taxable on any amount not allocated to the unitholders. The shareholders of CPPI will participate pro-rata in any dividends from CPPI. It is the current intention of CPPI to designate any dividends paid on CPPI Shares to be "eligible dividends" to the extent permitted by the Canadian Income Tax Act such that individuals would benefit from the enhanced gross-up and dividend tax credit mechanism under the Canadian Income Tax Act.

### SELECTED QUARTERLY FUND FINANCIAL INFORMATION

(thousands of dollars, except per unit amounts, unaudited)	<b>Q4 2010</b>	Q3 2010	Q2 2010	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009
Equity income (loss) in Canfor Pulp Limited Partnership	<b>23,867</b>	27,124	21,430	16,222	7,562	9,098	724	(10,740)
Net income (loss)	<b>23,935</b>	27,901	22,111	16,544	6,903	8,497	4,406	(10,740)
Net income (loss) per Fund unit	<b>\$0.67</b>	\$0.79	\$0.62	\$0.47	\$0.20	\$0.24	\$0.12	\$(0.30)
Distributions earned from the Partnership and declared to unitholders	<b>37,268</b>	24,491	18,457	11,357	4,969	1,065	1,065	2,130
Distributions declared per Fund unit	<b>\$1.05</b>	\$0.69	\$0.52	\$0.32	\$0.14	\$0.03	\$0.03	\$0.06
Partnership adjusted distributable cash per unit <sup>1</sup>	<b>\$0.68</b>	\$0.78	\$0.88	\$0.57	\$0.31	\$0.16	\$0.02	\$(0.06)

Note: <sup>1</sup> Represents the Partnership's adjusted distributable cash on which the Fund was dependent to make its own distributions. For further details on the Partnership's adjusted distributable cash see the Partnership's disclosure on pages 20 and 21.

Equity income (loss) in Canfor Pulp Limited Partnership represents the Fund's share of the Partnership's net income (loss). Net income (loss) is also impacted by future income tax expense (recovery) which is primarily influenced by changes in substantively enacted tax rates and the difference between the tax basis of the Fund's pro-rata ownership of the Partnership's assets and liabilities and the respective amounts reported in the financial statements.

## **OPERATING RESULTS AND LIQUIDITY**

For the quarter ended December 31, 2010, the Fund had net income of \$23.9 million or \$0.67 per Fund unit. The net income was the Fund's share of the Partnership's net income for the quarter and also includes a future income tax recovery of \$0.1 million. The future income tax recovery represents an adjustment to the future income tax liability based on the Fund's share of the differences between accounting and income tax values of the Partnership's assets and liabilities. The Fund's equity income in the Partnership decreased \$3.3 million when compared to the prior quarter. The decrease was primarily attributable to the Fund's share of lower operating earnings and lower income from non-operating items of the Partnership. The Fund's share of operating earnings of the Partnership decreased by \$2.7 million as a result of lower realized prices in Canadian dollar terms and higher unit manufacturing costs, partially offset by higher sales volumes. The Fund's share of non-operating items of the Partnership was \$0.6 million and was primarily the result of the foreign exchange gain on translation of US dollar denominated long-term debt and a net gain on derivative financial instruments, partially offset by a foreign exchange loss on working capital and interest expense.

Distributions declared by the Partnership and accruing to the Fund were \$37.3 million of which \$19.5 million was receivable at December 31, 2010. Cash distributions received from the Partnership were the only source of liquidity for the Fund. The Fund's requirements for administrative services were minimal and were funded and expensed by the Partnership. For further information refer to the Partnership's discussion of operating results and liquidity on pages 9 through 15 of this press release.

## **FUND DISTRIBUTIONS**

The Fund was entirely dependent on distributions from the Partnership to make its own distributions and declared distributions on a monthly basis with the record date on the last business day of each month and payable within the 15 days following. Distributions payable by the Partnership to the Fund and distributions payable by the Fund to its unitholders were recorded when declared. During the fourth quarter of 2010, the Fund declared distributions of \$1.05 per Fund unit or \$37.3 million.

Monthly cash distributions from the Partnership were not directly equal to the Fund's pro-rata share of the Partnership's income (loss) under the equity method. This was primarily due to capital expenditures, foreign exchange gains or losses on translation of US dollar denominated debt, changes in value of derivative instruments, amortization, and other non-cash expenses of the Partnership.

## **RISKS AND UNCERTAINTIES**

The Fund was subject to certain risks and uncertainties related to the nature of its investment in the Partnership and the structure of the Fund, as well as all of the risks and uncertainties related to the business of the Partnership. A comprehensive discussion of these risks and uncertainties is contained in the Fund's Annual Information Form dated February 18, 2010, which is available on [www.sedar.com](http://www.sedar.com) and [www.canforpulp.com](http://www.canforpulp.com).

## **CPPI SHARES**

At February 8, 2011, there were a total of 35,493,505 CPPI shares outstanding as a result of the aforementioned conversion of the Fund on January 1, 2011.

## **RELATED PARTY TRANSACTIONS**

All accounting, treasury, legal and administrative functions for the Fund were performed on its behalf, without charge, by the Partnership pursuant to a support agreement. Distributions earned from the Partnership for the three months ended December 31, 2010 were \$37.3 million of which \$17.8 million was received, with the balance of \$19.5 million receivable on December 31, 2010.

## **CRITICAL ACCOUNTING ESTIMATES**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements. Management regularly reviews these estimates and assumptions based on currently available

information. Significant areas requiring the use of management's estimates are the determination of future income taxes, and assessing whether there has been an other than temporary decline in the value of the investment in the Partnership. The determination of the future income tax liability requires management to estimate the future impacts of the Partnership's amortization of capital assets, capital cost allowance claims for tax purposes, and changes to actuarial estimates of employee benefit plans. The Fund accounted for its investment in the Partnership using the equity method. The Fund analyzed the carrying value of its investment in the Partnership by considering the underlying value of the Partnership's business. This assessment included various long-term assumptions related to the Partnership's operations which may not be reflected in the current market value of the Fund. Changes in these estimates could have a material impact on the calculation of the future income tax liability or equity investment in the Partnership.

## **INCOME TRUST CONVERSION RULES**

On June 12, 2007, legislation was substantively enacted whereby distributions made by publicly traded income trusts and partnerships will be taxed similar to that of income earned and distributed by a corporation. The Specified Investment Flow-Through Trust (SIFT) Tax became effective on January 1, 2011. On March 12, 2009 the Canadian government enacted legislation (SIFT Conversion Rules) which enables the conversion of a SIFT into a corporation on a tax-free rollover basis, prior to 2013.

The conversion of the Fund into a dividend paying public corporation named Canfor Pulp Products Inc. (CPPI) has been completed effective January 1, 2011 under the previously announced plan of arrangement approved by unitholders in April 2010. Under the arrangement, unitholders of the Fund received, for each unit of the Fund held, one common share of CPPI.

## **CONVERSION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS**

On February 13, 2008, the Accounting Standards Board announced that publicly accountable entities will be required to prepare financial statements in accordance with International Financial Reporting Standards (IFRS) for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. CPPI (as the continuing operations of the Canfor Pulp Income Fund) converted to IFRS effective January 1, 2011.

CPPI will rely on the resources of the Partnership to ensure compliance with IFRS. The Partnership will continue to review all proposed and continuing projects of the International Accounting Standards Board to determine their impact on CPPI, and will continue to invest in training and resources to ensure CPPI is making the appropriate judgments and following the IFRS accounting policies selected.

A detailed IFRS transition analysis has been substantively completed for CPPI and no significant changes compared to Canadian GAAP are expected for CPPI's 2011 consolidated financial statements other than potentially more detailed disclosure requirements.

The impact on CPPI's future financial position and results of operations is primarily dependent on changes in accounting policies that may materially impact the Partnership's consolidated financial statements.

For further details on the Partnership's transition plan see the Partnership's disclosure on pages 16 through 19.

The Partnership is currently finalizing its analysis to determine the significant IFRS transition impacts on the Fund's IFRS Opening Balance Sheet and the 2010 comparative numbers prior to conversion to a Corporation (CPPI). As a result of the specific characteristics of an Income Fund, the Partnership is focusing on the impact of International Accounting Standard (IAS) 32 "Financial Instruments: Presentation" and IAS 12 "Income Taxes" on the Fund's Opening Balance Sheet and the 2010 comparative numbers.

As a result of the conversion to a corporation effective January 1, 2011, the items discussed below will not be expected to have a material impact on CPPI's 2011 consolidated financial statements:

- While under Canadian GAAP the Fund units were classified as equity, the Partnership expects that IAS 32 will require that the Fund units be classified as a current financial liability under IFRS prior to conversion to a Corporation.

- Under Canadian GAAP the Fund recorded temporary tax differences that are expected to reverse after 2010 based on specified investment flow through entity ("SIFT") tax rates. However, IAS 12 requires that companies should generally use the "undistributed" rate for recording taxes. Therefore, under IFRS the rate to apply to temporary differences existing on January 1, 2010 that are expected to reverse after 2010 would be the highest marginal personal tax rate rather than the SIFT rate. The highest marginal personal tax rate is the rate at which tax would be payable by the Fund should distributions not be declared. Subsequent to January 1, 2011 as a result of the conversion of the Fund into a Corporation, the temporary tax differences are to be measured at the corporate tax rate.

## CANFOR PULP LIMITED PARTNERSHIP

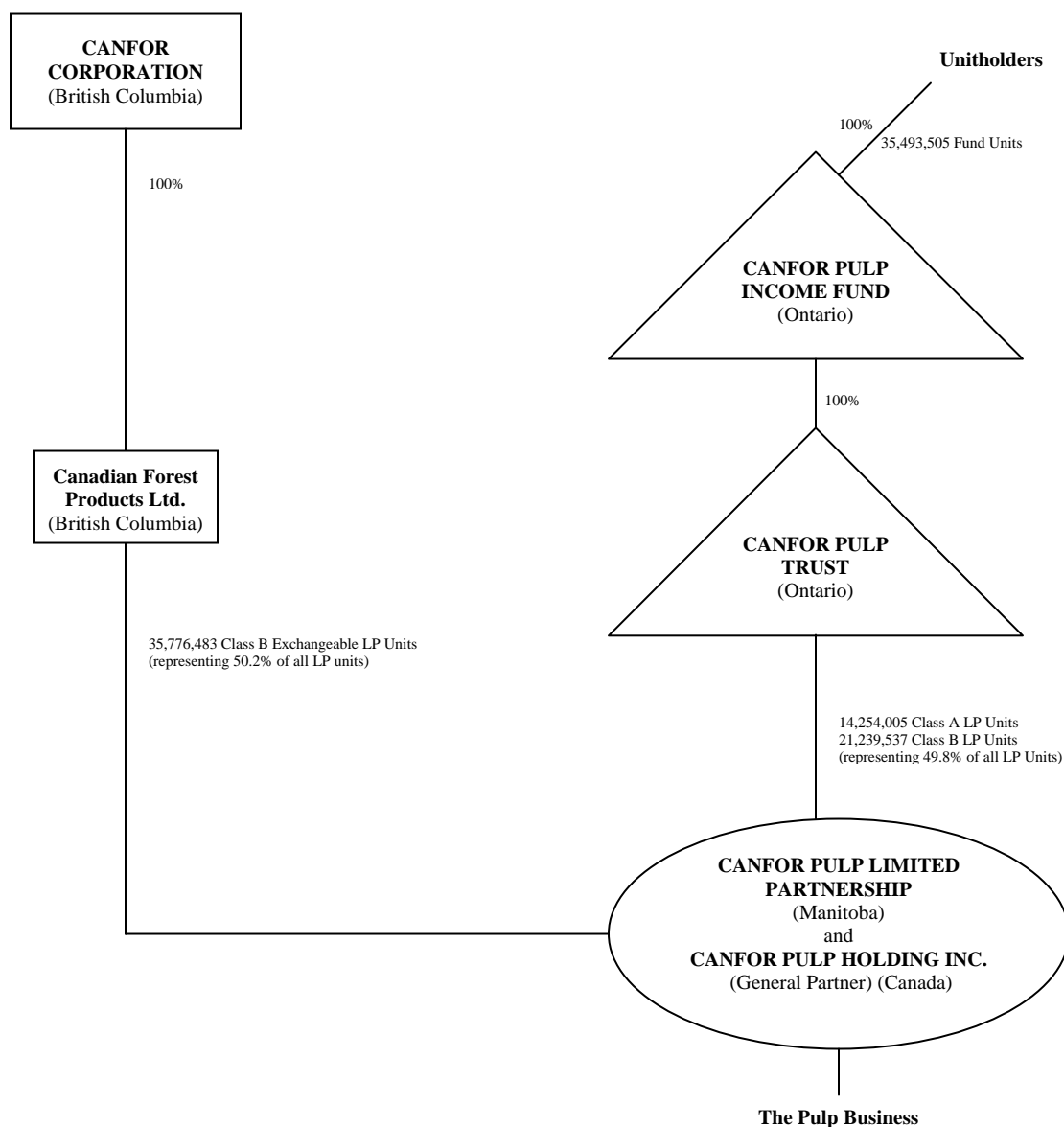
### Structure

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

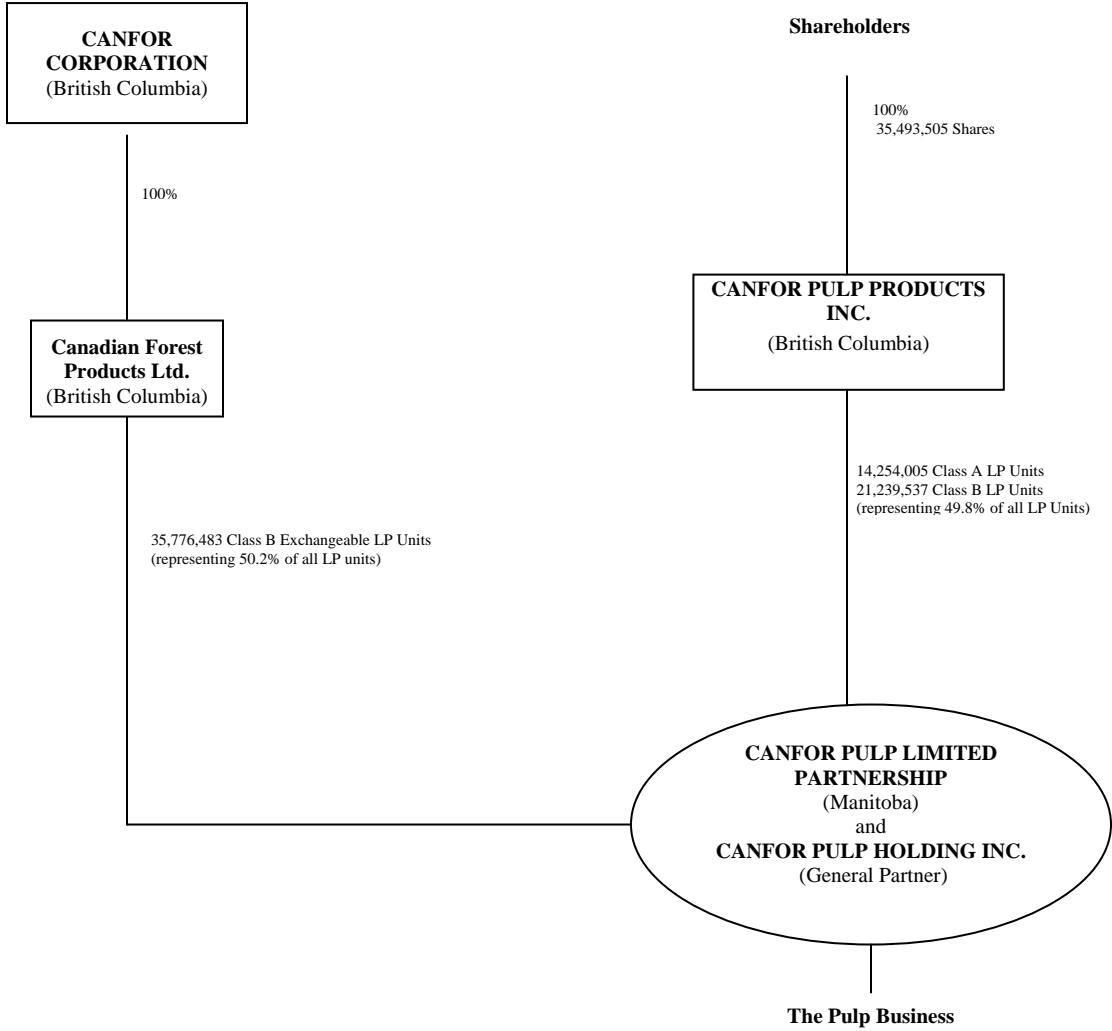
The conversion of the Fund into a dividend paying public corporation named Canfor Pulp Products Inc. (CPPI) has been completed effective January 1, 2011 under the previously announced plan of arrangement approved by unitholders in April 2010. Under the arrangement, unitholders of the Fund received, for each unit of the Fund held, one common share of CPPI. Below are simplified schematics of the ownership structure as at December 31, 2010 and after the conversion as at January 1, 2011.

At February 8, 2011, CPPI indirectly held a total of 14,254,005 Class A Limited Partnership Units and 21,239,537 Class B Limited Partnership Units, representing 49.8% of the Partnership and Canfor owns the remaining 50.2%. The Partnership is managed, on behalf of the limited partners, by Canfor Pulp Holding Inc., the General Partner.

### Ownership Structure as at December 31, 2010



**Ownership Structure as at January 1, 2011**





## The Business

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

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

## SUMMARY OF SELECTED PARTNERSHIP RESULTS

(millions of dollars, except for per unit amounts, unaudited)	<b>Q4 2010</b>	Q3 2010	<b>Year 2010</b>	Q4 2009	Year 2009
Sales	<b>266.1</b>	247.9	<b>1,001.1</b>	220.2	813.5
EBITDA <sup>1</sup>	<b>58.6</b>	63.6	<b>230.0</b>	27.3	61.8
Operating income	<b>46.6</b>	52.0	<b>182.7</b>	14.4	12.0
Net income	<b>47.9</b>	54.5	<b>178.0</b>	15.2	13.4
Per Partnership unit, basic and diluted					
Net income	<b>\$0.68</b>	\$0.76	<b>\$2.50</b>	\$0.21	\$0.19
EBITDA	<b>\$0.83</b>	\$0.89	<b>\$3.23</b>	\$0.39	\$0.87
Average exchange rate (US\$/Cdn\$) <sup>2</sup>	<b>0.987</b>	0.962	<b>0.971</b>	0.947	0.876

Notes: <sup>1</sup> For calculation of EBITDA, see supplementary financial information on page 20.

<sup>2</sup> Source – Bank of Canada (average noon rate for the period).

EBITDA for the fourth quarter of 2010 of \$58.6 million was \$5.0 million lower when compared to the third quarter of 2010 and was \$31.3 million higher when compared to the fourth quarter of 2009. The decrease when compared to the third quarter of 2010 was attributable to lower realized pulp prices and higher unit manufacturing costs, partially offset by higher shipment volumes. Realized pulp prices in Canadian dollar terms decreased 5% due to a 3% decrease in NBSK pulp US dollar list price and the impact of the stronger Canadian dollar. Unit manufacturing costs increased 3% when compared to the prior quarter as the impact of higher spending on fixed costs was partially offset by the impact of higher production volumes and lower fibre costs. The decrease in fibre costs when compared to the prior quarter was due to a decrease in the price of sawmill residual chips and whole log chips. Shipment volumes of the Partnership's pulp and paper products increased by 11% when compared to the prior quarter as a result of strong global demand, predominantly from China.

When compared to the fourth quarter of 2009, the \$31.3 million increase in EBITDA was primarily attributable to higher realized prices for the Partnership's pulp and paper products and higher shipment volumes, partially offset by higher unit manufacturing costs. Realized pulp prices in Canadian dollar terms increased by 15% as an 18% increase in NBSK pulp US dollar list prices and an increase in the proportion of sales into higher margin business, was partially offset by a 4% strengthening of the Canadian dollar. Realized paper prices in Canadian dollar terms increased by 24% when compared to the fourth quarter of 2009 due to strong paper demand and a higher proportion of prime grade sales in the fourth quarter of 2010. Higher unit manufacturing costs were the result of higher fibre costs, partially offset by the impact of higher production volumes.

For the full year 2010, EBITDA of \$230.0 million increased by \$168.2 million when compared to 2009. The increase in 2010 results were primarily attributable to higher realized prices for the Partnership's pulp and paper products and higher energy sales, partially offset by higher fibre costs. Realized pulp prices in Canadian dollar terms were 25% higher when compared to 2009 as a 34% increase in NBSK pulp US dollar list prices and increased sales volume into higher margin end uses, were partially offset by an 11% strengthening of the Canadian dollar. Realized paper prices in Canadian dollar terms increased 9% when compared to 2009. Unit manufacturing costs increased marginally when compared to 2009 due to higher fibre costs, partially offset by the impact of higher production volumes. Fibre costs increased 8% when compared to 2009 due to higher prices for sawmill residual chips which are partly tied to pulp

prices, partially offset by a reduction in the price and volume of whole log chips. Energy sales increased when compared to 2009 as the energy agreement with B.C. Hydro effective September 2009, was in effect for the full year 2010. Non-operating charges, included in net income of the Partnership totaled \$4.7 million in 2010, which represents an increase of \$6.1 million when compared to 2009. The increase in non-operating charges is primarily the result of a reduction in foreign exchange gain on translation of US dollar denominated long-term debt, partially offset by gains on financial derivative instruments, a reduction in foreign exchange losses on working capital and lower net interest expense.

## OPERATING RESULTS BY BUSINESS SEGMENT

### Pulp

(millions of dollars unless otherwise noted, unaudited)	Q4 2010	Q3 2010	Year 2010	Q4 2009	Year 2009
Sales	224.7	212.9	857.2	186.9	690.0
EBITDA	58.6	67.9	242.1	29.9	57.9
EBITDA margin	26%	32%	28%	16%	8%
Operating income	47.4	57.2	198.1	17.9	11.7
Average NBSK pulp list price – (US\$ per tonne, delivered to USA)	967	1,000	960	820	718
Average NBSK pulp list price – (Cdn\$ per tonne, delivered to USA)	980	1,040	989	866	820
Production – pulp (000 mt)	261.4	253.0	1,032.0	251.9	1,006.8
Shipments – Partnership-produced pulp (000 mt)	272.3	246.0	1,039.0	258.6	1,044.6
Marketed on behalf of HSLP & Canfor (000 mt)	58.8	116.1	457.8	126.1	521.7

The fourth quarter 2010 operating income for the pulp segment of \$47.4 million was a \$9.8 million decrease when compared to the third quarter of 2010. The reduction in operating earnings was attributable to lower realized prices and higher unit manufacturing costs, partially offset by higher shipment volumes. Realized pulp prices in Canadian dollar terms decreased 5% due to a 3% decrease in NBSK pulp US dollar list price and the impact of the stronger Canadian dollar. Unit manufacturing costs increased 3% when compared to the prior quarter as the impact of higher maintenance and energy costs were partially offset by the impact of higher production volumes and lower fibre costs. The decrease in fibre costs when compared to the prior quarter was due to a decrease in the price of sawmill residual chips and whole log chips. Shipment volumes of the Partnership's pulp products increased by 11% when compared to the prior quarter as a result of strong global demand, predominantly from China.

Operating income of the pulp segment in the fourth quarter of 2010 increased by \$29.5 million when compared to the same period a year ago, due to higher NBSK pulp US dollar list prices and higher sales volumes, partially offset by a stronger Canadian dollar and higher unit manufacturing costs. Realized pulp prices in Canadian dollar terms increased by 15% as an 18% increase in NBSK pulp US dollar list prices and a higher proportion of sales into higher margin business, primarily in China, was partially offset by a 4% strengthening of the Canadian dollar. Higher unit manufacturing costs were the result of higher fibre costs, partially offset by the impact of higher production volumes, and reduced natural gas consumption. Fibre costs increased 18% due to higher prices for sawmill residual chips, which are tied to the price of pulp, partially offset by reductions in the cost and volume of whole log chips. Energy sales under the terms of the Energy Purchase Agreement with BC Hydro totaled \$1.9 million, unchanged from the fourth quarter of 2009.

For the year ended December 31, 2010, operating income of \$198.1 million was \$186.4 million higher than in 2009. The improved operating results were attributable to higher realized pulp prices and higher energy sales, partially offset by higher unit manufacturing costs. Realized pulp prices in Canadian dollar terms were 25% higher when compared to 2009 as a 34% increase in NBSK pulp US dollar list price and increased sales volumes into higher margin end uses, were partially offset by an 11% stronger Canadian dollar. Energy sales under the terms of the Energy Purchase Agreement with BC Hydro totaling \$5.4 million in 2010 (2009 – \$1.9 million) were included in the pulp segment sales. Unit manufacturing costs increased by 1% when compared to 2009 as a result of higher fibre and maintenance costs, which were partially offset by the impact of higher production volumes and lower chemical

costs. Fibre costs increased 8% when compared to 2009 due to higher prices for sawmill residual chips which are partly tied to pulp prices, partially offset by a reduction in the price and volume of higher cost whole log chips. Market pulp production increased by 25,200 tonnes or 3%, and was mainly the result of strong operating rates at all facilities. Sales volumes of NBSK market pulp decreased 5,600 tonnes when compared to 2009 as a reduction in shipments to China were partially offset by increased shipments to North America.

### *Operations*

An average daily production rate record was achieved on a combined basis for the Partnership's facilities in 2010, exceeding the previous record set in 2007 by 2%. In addition, the Northwood and Intercontinental Pulp Mills surpassed previous records for average daily production rates.

NBSK market pulp production during the fourth quarter of 2010 was 8,400 tonnes higher than the third quarter of 2010, and 9,500 tonnes higher than the fourth quarter of 2009. The increased production when compared to the prior quarter was a result of the extended maintenance outage at the Northwood Pulp Mill in the third quarter of 2010. The increased production when compared to the same period in 2009 was the result of overall higher operating rates in the fourth quarter of 2010 and the impact of a scheduled maintenance outage at the Northwood Pulp Mill in the fourth quarter of 2009.

NBSK market pulp production during 2010 was 25,200 tonnes higher than in 2009. The increased production was mainly attributable to a 4% increase in the average daily production rate in 2010, partially offset by an overall reduction in operating days in 2010 due to extended maintenance outages at the Prince George and Northwood Pulp Mills.

### *Markets – Pulp*

Strong global softwood demand in the fourth quarter of 2010, led by China, allowed inventories held by producers and customers to decrease to low levels. According to the World 20<sup>1</sup> report, world pulp shipments hit an all time high in December 2010 and were 15% stronger than in December 2009. Pulp and Paper Products Council (PPPC) statistics reported an increase in global demand for printing and writing papers of 6% for full year 2010 as compared to 2009. PPPC reported an increase in global production for tissue of 1% for November year-to-date 2010 as compared to the same period in 2009.

The improvement in consumption resulted in decreasing global softwood inventories through the fourth quarter of 2010. At the end of December 2010, World 20<sup>1</sup> producers of bleached softwood pulp inventories were at 25 days of supply. By comparison, September 2010 inventories were at 27 days of supply. Market conditions are generally considered balanced when inventories fall in the 27-30 days of supply range.

As a result of these tight market conditions, producers were successful at mitigating pressure to reduce prices from the peak of US\$1,020 in the second quarter of 2010. Modest downward pressure was exerted on pricing in the latter half of 2010 with the restarts of the majority of the Chilean pulp mills after the earthquake and two idled North American mills. North American NBSK pulp list prices closed 2010 at US\$960 per tonne representing a US\$30 per tonne decrease from September 2010, but an increase of US\$110 per tonne or 13% when compared to the same period in 2009. In contrast, China NBSK pulp list prices increased from US\$820 in September 2010 to US\$830 in December 2010, driven by strong demand from that region.

Note: <sup>1</sup> World 20 data is based on twenty producing countries representing 80% of world chemical market pulp capacity and is based on information compiled and prepared by the Pulp and Paper Products Council.

### *Outlook – Pulp*

The global softwood pulp market is expected to remain balanced through the first quarter of 2011 with inventory stocks in a range that is expected to support current pricing levels. Demand remains solid with continued strong shipments into China and sustained demand in the North America Printing and Writing paper sector. Pulp mill operating rates are expected to increase in January and February with minimal scheduled downtime and as previously idled mills reach full capacity. However, in the second quarter of 2011, annual maintenance downtime coupled with extended outages due to several large capital projects in Canada funded under the Canadian Federal

government Green Transformation Program, are expected to curtail supply. Any relative weakness of the US dollar versus the Canadian dollar and the Euro is expected to exert upward pressure on US dollar list prices.

There are no scheduled maintenance outages planned for the first quarter of 2011. Scheduled maintenance outages are planned at the Prince George and Intercontinental Pulp Mills in the second quarter of 2011 with an estimated 10,000 tonnes of reduced production. A maintenance outage is planned at the Northwood Pulp Mill in the third quarter of 2011 which will be extended to complete work and commissioning of the recovery boiler upgrade project funded under the Canadian Federal government's Green Transformation Program, with a total of 40,000 tonnes of estimated reduced production.

## Paper

(millions of dollars unless otherwise noted, unaudited)	<b>Q4 2010</b>	Q3 2010	<b>Year 2010</b>	Q4 2009	Year 2009
Sales	<b>40.9</b>	34.7	<b>142.6</b>	32.3	122.5
EBITDA	<b>2.1</b>	1.0	<b>3.5</b>	0.9	13.9
EBITDA margin	<b>5%</b>	3%	<b>2%</b>	3%	11%
Operating income	<b>1.4</b>	0.2	<b>0.5</b>	0.1	10.6
Production – paper (000 mt)	<b>34.7</b>	34.7	<b>136.7</b>	38.4	131.0
Shipments – paper (000 mt)	<b>39.0</b>	33.6	<b>144.7</b>	38.1	135.0

The fourth quarter 2010 operating income of the paper segment improved \$1.2 million when compared to the third quarter of 2010, and was \$1.3 million higher when compared to the same period last year. The increase when compared to the third quarter of 2010 was primarily attributable to lower unit manufacturing costs, higher realized paper prices in Canadian dollar terms and higher sales volumes. The lower unit manufacturing costs were the result of lower prices for slush pulp partially offset by higher spending on fixed costs. The slush pulp is transferred to the paper segment at a market price with the decrease directly attributable to the decrease in the realized pulp price in Canadian dollar terms. Realized prices in Canadian dollar terms increased by approximately 1%.

When compared to the fourth quarter of 2009 the increase in operating earnings was due to a 24% increase in realized paper prices in Canadian dollar terms, partially offset by higher unit manufacturing costs. The increase in paper prices were due to improved demand and pressure to raise paper prices as margins of paper makers eroded with the substantial increase in global pulp prices through the latter half of 2009 to mid 2010. Increased unit manufacturing costs were primarily attributable to higher costs for slush pulp and the impact of lower production volumes, partially offset by lower spending on fixed costs. Sales volumes increased slightly in the fourth quarter of 2010 due to solid demand.

For the full year, 2010 paper segment operating results declined by \$10.1 million when compared to 2009. The decrease was primarily attributable to higher costs for slush pulp, partially offset by a 9% increase of realized prices in Canadian dollar terms and higher shipment volumes. Slush pulp costs, which are transferred to the paper segment at market price, increased 35% when compared to 2009. Partially offsetting the higher slush pulp costs was the impact of higher production volumes on unit costs. Paper shipments increased by 7% when compared to 2009.

## Operations

Paper production for the fourth quarter of 2010 was 34,700 tonnes, unchanged when compared to the third quarter of 2010. When compared to the same period in the prior year, production was 3,700 tonnes lower due to lower operating days in the fourth quarter of 2010.

The paper division produced a record 136,700 tonnes in 2010, an increase of 5,700 tonnes when compared to 2009. The increase was attributable to a record average daily production rate achieved in 2010 and an increase in operating days, mainly attributable to the impact of the market curtailment, which commenced in the third week of December 2008 and extended into January 2009.

## Markets

Kraft paper demand remained strong through the end of the year and paper markets were balanced with supply. American Forest and Paper Association reported that US total Kraft paper shipments for December 2010 were unchanged from November and increased 1% when compared to December 2009. Full year 2010 shipments were 10% higher when compared to 2009. The Pulp Shipping Sack Manufacturers' Association shipping sack statistics for December reveal that industry paper consumption was up 3% from the previous month, and increased 7% for full year 2010 when compared to 2009. During the latter half of 2010, North American prices remained relatively stable while export prices continued to increase.

The Partnership's prime paper shipments in the fourth quarter of 2010 increased 18% from the third quarter of 2010. For the full year 2010, prime paper shipments increased 11% and prime bleached shipments increased by 32% when compared to 2009.

## Outlook – Kraft Paper

Kraft paper demand is currently strong and the supply/demand balance is expected to remain positive through the first quarter of 2011. Prices are expected to remain stable through the first quarter of 2011 with some potential for modest price increases as higher than expected consumer spending in the latter half of 2010 is representative of demand growth which may provide pricing momentum heading into 2011. The Partnership's prices in US dollar terms are vulnerable to the relative strength of the Canadian dollar in relation to other currencies, primarily the US dollar.

## Non-Segmented Costs

(millions of dollars, unaudited)	<b>Q4 2010</b>	Q3 2010	<b>Year 2010</b>	Q4 2009	Year 2009
Unallocated costs	<b>2.2</b>	5.4	<b>15.9</b>	3.6	10.3
Interest expense, net	<b>1.9</b>	2.0	<b>7.8</b>	2.2	10.1
Foreign exchange gain on long-term debt	<b>(3.9)</b>	(3.4)	<b>(5.7)</b>	(2.9)	(19.6)
Loss (gain) on derivative financial instruments	<b>(2.3)</b>	(2.6)	<b>(1.5)</b>	(0.5)	1.5
Foreign exchange loss on working capital	<b>2.8</b>	1.5	<b>4.0</b>	0.5	6.7
Other expense (income)	<b>0.2</b>	-	<b>0.1</b>	(0.1)	(0.1)
	<b>0.9</b>	2.9	<b>20.6</b>	2.8	8.9

## Unallocated Costs

Unallocated costs, comprised principally of general and administrative expenses, totaled \$2.2 million in the fourth quarter of 2010 compared to \$5.4 million in the third quarter of 2010 and \$3.6 million in the fourth quarter of 2009. The reduction in unallocated costs when compared to the third quarter was primarily attributable to a one-time fee received in respect of the termination of the agency sales agreement with Howe Sound Limited Partnership (HSLP) due to the sale by Canfor of their ownership interest in HSLP, partially offset by expenses incurred to convert to a corporation on January 1, 2011.

For the full year 2010, unallocated costs totaled \$15.9 million compared to \$10.3 million for the same period in 2009. The increased costs were primarily attributable to higher accruals for performance based incentive plans, higher consulting costs and corporate conversion expenses, which were partially offset by a one-time fee received in respect of the termination of the agency sales agreement with HSLP due to the sale by Canfor of its ownership interest in HSLP.

## Interest Expense

For the fourth quarter of 2010 the net interest expense remained relatively unchanged from the prior quarter.

### Other Non-segmented Items

The foreign exchange gain on long-term debt of \$3.9 million resulted from translating the US\$110 million debt at period-end exchange rates, reflecting the stronger Canadian dollar as of December 31, 2010.

The foreign exchange loss on working capital of \$2.8 million resulted from translating US dollar balances at period-end exchange rates.

The net gain of \$2.3 million on derivative financial instruments recorded in the fourth quarter of 2010 relates to the revaluation to market of outstanding contracts at the end of the quarter for natural gas swaps and US dollar forward contracts, partially offset by the settlement of maturing contracts during the quarter. The revaluation to market of outstanding derivative instruments recorded in the quarter resulted in a gain of \$1.4 million and relates to a revaluation to market of outstanding natural gas swaps and outstanding US dollar forward contracts at the end of the quarter. A loss of \$1.1 million on settlement of natural gas swaps was recorded in the fourth quarter of 2010. The natural gas swaps are used to fix the price on a portion of the Partnership's future natural gas requirements. In the fourth quarter of 2010 the Partnership recorded a net gain of \$2.0 million on settlement of US dollar forward contracts to hedge the impact of currency fluctuations on US dollar working capital.

### SUMMARY OF FINANCIAL POSITION

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

(millions of dollars, except for ratios, unaudited)	December 31, 2010		December 31, 2009	
Ratio of current assets to current liabilities	1.96		2.04	
Ratio of net debt to partners' equity <sup>1</sup>	0.09		0.19	

	Q4 2010	Year 2010	Q4 2009	Year 2009
Increase (decrease) in cash and cash equivalents	36.7	50.7	(30.4)	13.1
Comprised of cash flow from (used in):				
Operating activities	89.3	219.6	(22.5)	71.2
Financing activities	(53.5)	(150.4)	(5.0)	(40.9)
Investing activities	0.9	(18.5)	(2.9)	(17.2)

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

### Changes in Financial Position

Cash generated from operating activities was \$89.3 million in the fourth quarter of 2010 compared to cash used in operating activities of \$22.5 million in the fourth quarter of 2009. The increase in cash generated from operating activities is the result of an increase in cash generated from working capital and improved operating earnings. The increase of cash generated from working capital during the fourth quarter of 2010 was primarily the result of reductions in the volume of finished goods and chip inventories, a decrease in prepaid balances relating to the timing of scheduled maintenance outages and timing of payments and receipts. The increase in cash generated from operations was primarily attributable to higher realized prices in Canadian dollar terms for the Partnership's pulp and paper products and higher shipment volumes, partially offset by higher unit manufacturing costs.

The cash used in financing activities of \$53.5 million in the quarter represents distributions paid to the limited partners, namely Canfor and the Fund.

The cash generated from investing activities in the quarter is comprised of \$19.1 million of funds received for claims under the Canadian Federal government's Green Transformation Program, partially offset by \$18.2 million relating to capital expenditures.

## **FINANCIAL REQUIREMENTS AND LIQUIDITY**

At December 31, 2010 the Partnership had outstanding long-term debt of \$109.4 million (2009 – \$115.1 million, US\$110.0 million for both 2010 and 2009) in the form of unsecured US dollar private placement notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013.

At the end of the year, the Partnership had cash and cash equivalents of \$64.2 million, of which \$39.2 million was used to pay declared distributions on January 14, 2011. The Partnership has a \$40.0 million bank credit facility with a maturity date of November 30, 2011, of which \$0.5 million was utilized at December 31, 2010 for a standby letter of credit issued for general business purposes. In addition, the Partnership has a separate facility with a maturity date of November 30, 2011, to cover the \$13.2 million standby letter of credit issued to BC Hydro under the Energy Purchase Agreement. Interest and other costs of the bank credit facility are at prevailing market rates.

The Partnership manages cash resources to fund current and future operations through management of its capital structure in conjunction with cash flow forecasting, including anticipated investing and financing activities. The Partnership uses the bank credit facility to meet short-term working capital requirements. The Partnership also reviews on an ongoing basis, the level of distributions, capital expenditures and timing of scheduled major maintenance outages and may adjust these periodically to manage cash resources.

The Partnership periodically discounts letters of credit on outstanding trade receivables to reduce borrowing costs, to reduce credit and foreign currency exposure, and to increase short-term liquidity.

The Notes and bank credit agreements each contain similar financial covenants including a maximum allowable debt:EBITDA leverage ratio and minimum required EBITDA:interest coverage ratio. The Partnership remained in compliance with all covenants at December 31, 2010 and throughout the year.

On October 9, 2009 the Canadian Federal government announced the allocation of credits from the billion dollar Pulp and Paper Green Transformation Program (the Program). The Partnership has been allocated \$122.2 million from the Program announced by the Canadian government on June 17, 2009. The Program is designed as a reimbursement of funds to be spent on qualifying energy and environmental capital projects. Credits may be used until the Program end date of March 31, 2012. The Partnership has received Program approval to proceed with three projects totaling \$115.6 million. The Partnership expects to submit further projects over the balance of 2011. As of December 31, 2010 the Partnership has incurred \$38.1 million and received reimbursements totaling \$20.2 million with the balance of \$17.9 million receivable on December 31, 2010. The Partnership submits claims for expenditures on approved projects under the Program on a monthly basis. These projects are expected to provide economic and environmental benefits to the Partnership's operations.

## **OUTSTANDING UNITS**

At February 8, 2011, there were 71,270,025 Limited Partnership Units outstanding, of which 35,493,542 units (consisting of 14,254,005 Class A Limited Partnership Units and 21,239,537 Class B Limited Partnership Units) were owned by CPPI and 35,776,483 Class B Exchangeable Limited Partnership Units were owned indirectly by Canfor.

## **RELATED PARTY TRANSACTIONS**

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2009 audited consolidated financial statements and are based on agreed upon amounts, and are summarized in note 9 of the unaudited interim consolidated financial statements.

## **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

During the quarter ending December 31, 2010, there were no changes in the Partnership's internal controls over financial reporting that materially affected, or would be reasonably likely to materially affect, such controls.

## **RISKS AND UNCERTAINTIES**

A comprehensive discussion of risks and uncertainties is included in the Fund's Annual Information Form dated February 18, 2010, which is available on [www.sedar.com](http://www.sedar.com) and [www.canforpulp.com](http://www.canforpulp.com).

## SELECTED QUARTERLY PARTNERSHIP FINANCIAL INFORMATION

(millions of dollars unless otherwise noted, unaudited)	Q4 2010	Q3 2010	Q2 2010	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009
<b>Sales and Income</b>								
Sales	266.1	247.9	247.6	239.5	220.2	202.0	205.0	186.3
Operating income (loss)	46.6	52.0	51.6	32.5	14.4	12.4	(5.0)	(9.8)
EBITDA	58.6	63.6	63.7	44.1	27.3	25.1	7.2	2.2
Net income (loss)	47.9	54.5	43.1	32.5	15.2	18.3	1.5	(21.6)
<b>Per Partnership unit (dollars)</b>								
Net income (loss) basic and diluted	\$0.68	\$0.76	\$0.60	\$0.46	\$0.21	\$0.26	\$0.02	\$(0.30)
<b>Statistics</b>								
Pulp shipments (000 mt)	272.3	246.0	252.3	268.4	258.6	259.5	286.2	240.3
Paper shipments (000 mt)	39.0	33.6	34.4	37.7	38.1	37.4	34.3	25.2
Average exchange rate (US\$/Cdn\$) <sup>1</sup>	0.987	0.962	0.973	0.961	0.947	0.912	0.858	0.803
Average NBSK pulp list price – (US\$ per tonne, delivered to USA)	967	1,000	993	880	820	733	645	673
<b>Per Partnership unit (dollars)</b>								
Adjusted distributable cash per unit <sup>2</sup>	\$0.68	\$0.78	\$0.88	\$0.57	\$0.31	\$0.16	\$0.02	\$(0.06)
Distributions declared per unit	\$1.05	\$0.69	\$0.52	\$0.32	\$0.14	\$0.03	\$0.03	\$0.06

Notes: <sup>1</sup> Source – Bank of Canada (average noon rate for the period).

<sup>2</sup> For further details on the Partnership's adjusted distributable cash see the Partnership's disclosure on pages 20 and 21.

Sales are primarily influenced by changes in market pulp prices, sales volumes and fluctuations in Canadian dollar exchange rates. Operating income (loss), net income (loss) and EBITDA are primarily impacted by: the level of sales; freight costs; fluctuations of fibre, chemical, and energy prices; level of spending and the timing of scheduled maintenance downtime; and production curtailments. Net income (loss) is also impacted by fluctuations in Canadian dollar exchange rates, the market price of natural gas, the revaluation to the period end rate of US dollar denominated working capital balances and long-term debt, and revaluation of outstanding natural gas swaps and US dollar forward contracts.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements. On an ongoing basis, management reviews its estimates, including those related to asset useful lives for amortization, impairment of long-lived assets, pension and other employee future benefit plans and asset retirement obligations, based upon currently available information. While it is reasonably possible that circumstances may arise which cause actual results to differ from these estimates, management does not believe it is likely that any such differences will materially affect the Partnership's financial condition.

## CONVERSION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

### *Project Update*

On February 13, 2008, the Accounting Standards Board announced that publicly accountable entities will be required to prepare financial statements in accordance with International Financial Reporting Standards (IFRS) for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. The Partnership converted to these new standards effective January 1, 2011.

The Partnership has completed the detailed diagnostic activities of its transition plan. Differences between IFRS and Canadian generally accepted accounting principles (GAAP), in addition to those referenced below, may continue to be identified based on changes in IFRS prior to the release of the Partnership's first full set of financial statements in compliance with IFRS for the year ending December 31, 2011.

The process of converting to IFRS has been divided into a number of different stages, several which have run



concurrently. A number of accounting policy choices have been recommended by the Partnership's Steering Committee but have not been finalized. At December 31, 2010, the full impact the IFRS transition would have on the Partnership's financial statements could not be reasonably determined. The disclosures in this MD&A reflect the Partnership's expectations based on information available at December 31, 2010. Changes in IFRS standards or circumstances relating to the Partnership may cause the Partnership to revise its expectations and its potential IFRS accounting policy choices.

The Partnership anticipates additional disclosure resulting from the adoption of IFRS and has identified and assessed these additional disclosure requirements. No significant systems changes have been identified, that will be necessary to compile the required disclosures.

The Partnership does not expect that the transition to IFRS will have a significant impact on its financial covenants contained in the existing Notes and bank credit facility agreements.

#### *First-time Adoption of International Financial Reporting Standards (IFRS 1)*

At adoption of IFRS, an entity is required to apply IFRS 1, which provides guidance for an entity's initial adoption of IFRS. IFRS 1 generally requires an entity to apply all IFRS effective at the end of the first reporting period retrospectively. However, IFRS 1 provides certain mandatory exceptions and permits limited optional exemptions in specified areas of certain standards from this general requirement. The Partnership expects to take the following optional elections provided by IFRS 1. All other available elections are either not applicable or not material to the Partnership. Elections are subject to change as new information becomes available.

- **Borrowing costs:**

IAS 23, Borrowing Costs, requires the capitalization of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Under Canadian GAAP, you have an accounting policy choice to expense these costs as incurred or capitalize them. The Partnership expects to elect to apply the requirements of IAS 23 prospectively from January 1, 2010.

- **Employee Benefits:**

The Partnership expects to elect to recognize all cumulative actuarial gains and losses at the date of transition to IFRS. Actuarial gains and losses would have to be recalculated under IFRS from the inception of each of our defined benefit plans if the exemption is not taken.

- **Business combinations:**

The Partnership expects to apply the business combinations exemption in IFRS 1. Accordingly, the Partnership will not modify the carrying amounts of assets and liabilities arising on business combinations occurring before the transition date.

#### *Accounting Policies*

Below is a summary of expected changes to the Partnership's accounting policies for those standards which are expected to materially impact the Partnership's consolidated financial statements. The list and comments below should not be regarded as a final list of changes that will result from the transition to IFRS. It is intended to highlight the significant areas the Partnership has identified to date; however, some decisions are pending final approval where choices of accounting policies are available. Any changes to recognized financial figures may affect non-GAAP and performance measures including but not limited to, EBITDA and distributable cash.

<b>Accounting Policy Area</b>	<b>Impact of Policy Adoption</b>
Property, Plant and Equipment	<p><b>Choices:</b> Either a historical cost model or a revaluation model can be used to value property, plant and equipment.</p> <p><b>Policy Selection:</b> The Partnership will value property, plant and equipment using the historical cost model.</p>

Accounting Policy Area	Impact of Policy Adoption
Major Maintenance	<p><b>Choices:</b> There are no policy choices available under IFRS.</p> <p><b>Differences from existing Canadian GAAP:</b> For major maintenance, IAS 16 requires for major inspections and overhauls to be accounted as a separate component of PP&amp;E if the component is used for more than one reporting period. This treatment is only intended for major expenditures that occur at regular intervals over the life of the asset as costs of routine repairs and maintenance will continue to be expensed as incurred. The regularly scheduled major maintenance outages required on the Partnership's plant and equipment would likely qualify for treatment under this standard with the expenditures being classified as property, plant and equipment.</p> <p><b>Policy status:</b> As at January 1, 2010 under Canadian GAAP, expenditures during the Partnership's major maintenance outages are classified as prepaid expense and other assets (\$15.3 million), and other long-term assets (\$5.4 million), as appropriate and amortized over the period between scheduled major maintenance outages.</p> <p>The impact on the Partnership's opening balance sheet as at January 1, 2010 as a result of this treatment will be a decrease in the Partnership's prepaid expense and other assets, and other long-term assets, with a corresponding increase in PP&amp;E. In addition the Partnership's amortization will increase with a corresponding decrease in manufacturing and product costs, with no net impact to net income or operating income.</p>
Employee Benefits	<p><b>Choices:</b> Actuarial gains and losses are permitted under IAS 19, "Employee Benefits", to be recognized directly in other comprehensive income rather than through profit or loss.</p> <p><b>Policy Selection:</b> Actuarial gains and losses will be recognized in other comprehensive income.</p> <p><b>Differences from existing Canadian GAAP:</b> IAS 19 requires the past service cost element of defined benefit plans to be expensed on an accelerated basis, with vested past service costs expensed immediately and unvested past service costs recognized on a straight-line basis until the benefits become vested. Under Canadian GAAP, past service costs are generally amortized on a straight-line basis over the expected average remaining service period of active employees under the plan.</p> <p>Under Canadian GAAP, certain gains and losses which were unrecognized at the time of adopting the current Canadian accounting standard were permitted to be amortized over a period under transitional provisions of the current standard. Under IFRS, those amounts will not be permitted to remain unrecognized and must be recognized on transition to IFRS.</p> <p><b>Policy status:</b> The Partnership's actuarial valuation is currently being finalized under IFRS including potential IFRIC 14 adjustments and related accounting policy choices.</p>
Impairment of assets	<p><b>Choices:</b> There are no policy choices available under IFRS.</p> <p><b>Differences from existing Canadian GAAP:</b> Canadian GAAP generally uses a two-step approach to impairment testing: first comparing asset carrying values with undiscounted future cash flows to determine whether impairment exists; and then measuring any impairment by comparing asset carrying values with fair values. IAS 36, "Impairment of Assets", uses a one-step approach for both testing for and measurement of impairment, with asset carrying values compared directly with the higher of fair value less costs to sell and value in use (discounted cash flows). This may potentially result in more write downs where carrying values of assets were previously supported under Canadian GAAP on an undiscounted cash flow basis, but could not be supported on a discounted cash flow basis.</p> <p>In addition, the extent of any new write-downs may be partially offset by the requirement under IAS 36 to reverse any previous impairments where circumstances have changed</p>

Accounting Policy Area	Impact of Policy Adoption
	<p>such that the impairments have been reduced. Canadian GAAP prohibits reversal of impairment losses.</p> <p><b>Policy status:</b> Based on the Partnership's analysis no impairment charges under IFRS are necessary as at January 1, 2010.</p>
Provisions (Including Asset Retirement Obligations)	<p><b>Choices:</b> There are no policy choices available under IFRS.</p> <p><b>Differences from existing Canadian GAAP:</b> IAS 37, "Provisions, Contingent Liabilities and Contingent Assets", requires a provision to be recognized when there is a present obligation as a result of a past transaction or event; it is probable that an outflow of resources will be required to settle the obligation; and a reliable estimate can be made of the obligation, where "probable" in this context, means more likely than not. The criteria for recognition in the financial statements under Canadian GAAP, is "likely", which is a higher threshold than "probable". Therefore, it is possible that there may be some contingent liabilities which would meet the recognition criteria under IFRS that were not recognized under Canadian GAAP. Other differences between IFRS and Canadian GAAP exist in relation to the measurement of provisions, such as the methodology for determining the best estimate where there is a range of equally possible outcomes (IFRS uses the mid-point of the range, whereas Canadian GAAP uses the low-end of the range), and the requirement under IFRS for provisions to be discounted where material.</p> <p><b>Policy status:</b> The Partnership does not expect this change in accounting policy to have a significant impact as at January 1, 2010.</p>
Borrowing Costs	<p><b>Choices:</b> There are no policy choices available under IFRS.</p> <p><b>Differences from existing Canadian GAAP:</b> Under Canadian GAAP, an entity can choose whether to expense or capitalize borrowing costs, whereas IFRS requires qualifying borrowing costs to be capitalized.</p>
Statement of Cash Flows	<p><b>Choices:</b> Either the direct or the indirect method may be presented. Distributions and interest paid and interest received can be presented as operating, financing or investing activities respectively.</p> <p><b>Policy selection:</b> The Partnership expects to use the indirect method. Distributions and interest paid would be presented as financing activities and interest received would be presented as an investing activity.</p> <p><b>Differences from existing Canadian GAAP:</b> None</p>

#### *Post-Implementation*

The post-implementation work will involve continuous monitoring of changes in IFRS throughout the implementation process (through to the end of 2011). We note that the standard-setting bodies that determine Canadian GAAP and IFRS have significant ongoing projects that could impact the differences between Canadian GAAP and IFRS and their impact on our financial statements. In particular, we expect that there may be additional new or revised IFRS in relation to consolidation, joint ventures, financial instruments, hedge accounting, discontinued operations, leases and employee benefits. We have processes in place to ensure that potential changes are monitored and evaluated. The impact of any new IFRS will be evaluated as they are drafted and published.

#### *Disclosure Controls and Internal Controls over Financial Reporting*

Due to the fact that IFRS requires more judgment with respect to various accounting treatments additional or modified processes and controls have been put in place. These changes to financial reporting controls will ensure that the Partnership is making the appropriate judgments and adhering to the IFRS accounting policies selected.

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

	Three months ended		Year ended	
	December 31,	December 31,	December 31,	December 31,
(millions of dollars, unaudited)	2010	2009	2010	2009
<b>RECONCILIATION OF NET INCOME TO EBITDA</b>				
<b>Net income</b>	<b>\$ 47.9</b>	<b>\$ 15.2</b>	<b>\$ 178.0</b>	<b>\$ 13.4</b>
Add (deduct):				
Amortization	11.9	12.6	47.4	49.4
Net interest expense	1.9	2.2	7.8	10.1
Foreign exchange gain on long-term debt	(3.9)	(2.9)	(5.7)	(19.6)
Loss (gain) on derivative financial instruments	(2.3)	(0.5)	(1.5)	1.5
Foreign exchange loss on working capital	2.8	0.5	4.0	6.7
Other expense	0.3	0.2	-	0.3
<b>EBITDA</b>	<b>\$ 58.6</b>	<b>\$ 27.3</b>	<b>\$ 230.0</b>	<b>\$ 61.8</b>
<b>EBITDA per Partnership unit</b>	<b>\$ 0.83</b>	<b>\$ 0.39</b>	<b>\$ 3.23</b>	<b>\$ 0.87</b>

	Three months ended		Year ended	
	December 31,	December 31,	December 31,	December 31,
(millions of dollars, unaudited)	2010	2009	2010	2009
<b>CALCULATION OF STANDARDIZED AND ADJUSTED DISTRIBUTABLE CASH</b>				
<b>Cash flow from operating activities</b>	<b>\$ 89.3</b>	<b>\$ (22.5)</b>	<b>\$ 219.6</b>	<b>\$ 71.2</b>
Deduct: Capital expenditures – cash <sup>1</sup>	(3.9)	(2.9)	(12.0)	(17.3)
<b>Standardized distributable cash</b>	<b>\$ 85.4</b>	<b>\$ (25.4)</b>	<b>\$ 207.6</b>	<b>\$ 53.9</b>
<b>Adjustments to standardized distributable cash:</b>				
Add (deduct):				
Increase (decrease) in non-cash working capital	(36.9)	43.8	2.4	(31.8)
Net long-term deferred maintenance	(0.5)	3.5	(2.3)	4.6
Capital expenditure accruals – net	0.3	0.4	(0.6)	3.8
<b>Adjusted distributable cash</b>	<b>\$ 48.3</b>	<b>\$ 22.3</b>	<b>\$ 207.1</b>	<b>\$ 30.5</b>
Standardized distributable cash – per Partnership unit (in dollars)	\$ 1.20	\$ (0.35)	\$ 2.91	\$ 0.76
Adjusted distributable cash – per Partnership unit (in dollars)	\$ 0.68	\$ 0.31	\$ 2.91	\$ 0.43
<b>Cash distributions declared (paid and payable)</b>	<b>\$ 74.8</b>	<b>\$ 10.0</b>	<b>\$ 183.9</b>	<b>\$ 18.6</b>
Cash distributions declared – per Partnership unit (in dollars)	\$ 1.05	\$ 0.14	\$ 2.58	\$ 0.26

Note: <sup>1</sup> Presented net of Canadian Federal government Green Transformation Program expenditures.

**DISTRIBUTABLE CASH AND CASH DISTRIBUTIONS**

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

Adjusted distributable cash is defined as the standardized distributable cash prior to the effects of changes in non-cash working capital and long-term deferred maintenance, asset retirement obligation expenditures and accruals, and after provision for accrued capital expenditures.

The Board determines the level of cash distributions based on the level of cash flow from operations before changes in non-cash working capital and long-term deferred maintenance, asset retirement obligation expenditures and

accruals, less capital expenditures. During the year distributions are based on estimates of full year cash flow and capital spending; thus distributions may be adjusted as these estimates change. It is expected that normal seasonal fluctuations in working capital will be funded from cash resources or the revolving short-term credit facility.

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

(thousands of dollars, except unit and per unit amounts, unaudited)	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
<b>Income</b>				
Equity income in Canfor Pulp Limited Partnership	\$ 23,867	\$ 7,562	\$ 88,643	\$ 6,644
Net income before future income taxes	23,867	7,562	88,643	6,644
Future income tax (recovery) (note 6)	(68)	659	(1,848)	(2,422)
Net income	23,935	6,903	90,491	9,066
Distributions declared (note 4)	(37,268)	(4,969)	(91,573)	(9,229)
Earnings in excess of distributions – surplus (deficit)	\$ (13,333)	\$ 1,934	\$ (1,082)	\$ (163)
<b>Net income per unit, basic and diluted</b>	<b>\$ 0.67</b>	<b>\$ 0.20</b>	<b>\$ 2.55</b>	<b>\$ 0.26</b>
<b>Weighted average number of units</b>	<b>35,493,505</b>	<b>35,493,505</b>	<b>35,493,505</b>	<b>35,493,505</b>
<b>Accumulated Earnings and Distributions</b>				
Net income for the period	\$ 23,935	\$ 6,903	\$ 90,491	\$ 9,066
Equity interest in other comprehensive income (loss) of Canfor Pulp Limited Partnership	(6)	(30)	26	(45)
<b>Comprehensive income</b>	<b>\$ 23,929</b>	<b>\$ 6,873</b>	<b>\$ 90,517</b>	<b>\$ 9,021</b>
<b>Accumulated Earnings and Distributions</b>				
Balance, beginning of period – distributions in excess of earnings	\$ (60,775)	\$ (74,960)	\$ (73,026)	\$ (72,863)
Earnings in excess of distributions – surplus (deficit), current period	(13,333)	1,934	(1,082)	(163)
<b>Balance, end of period – Accumulated distributions in excess of earnings</b>	<b>\$ (74,108)</b>	<b>\$ (73,026)</b>	<b>\$ (74,108)</b>	<b>\$ (73,026)</b>

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

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

(thousands of dollars, unaudited)	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
<b>Cash generated from (used in)</b>				
<b>Operating activities</b>				
Net income	\$ 23,935	\$ 6,903	\$ 90,491	\$ 9,066
Items not affecting cash:				
Equity income in Canfor Pulp Limited Partnership	(23,867)	(7,562)	(88,643)	(6,644)
Future income tax (recovery)	(68)	659	(1,848)	(2,422)
Distributions received from Canfor Pulp Limited Partnership	26,620	2,485	74,891	7,809
	26,620	2,485	74,891	7,809
<b>Financing activities</b>				
Distributions paid to unitholders	\$ (26,620)	\$ (2,485)	\$ (74,891)	\$ (7,809)
<b>Beginning, change and ending balance in cash and cash equivalents</b>	\$ -	\$ -	\$ -	\$ -

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

# **Canfor Pulp Income Fund** **Consolidated Balance Sheets**

(thousands of dollars, unaudited)		As at December 31, 2010	As at December 31, 2009
<b>ASSETS</b>			
<b>Current assets</b>			
Distributions receivable from Canfor Pulp Limited Partnership (notes 4,5)	\$	19,521	\$ 2,839
Total current assets		19,521	2,839
Equity investment in Canfor Pulp Limited Partnership (note 3)		260,740	263,644
	\$	280,261	\$ 266,483
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Distributions payable (note 4)	\$	19,521	\$ 2,839
Total current liabilities		19,521	2,839
Future income taxes (note 6)		35,439	37,287
	\$	54,960	\$ 40,126
<b>UNITHOLDERS' EQUITY</b>			
Unitholders' equity – 35,493,505 Fund units outstanding	\$	299,351	\$ 299,351
Accumulated earnings and distributions		(74,108)	(73,026)
Accumulated other comprehensive income (note 7)		58	32
Total Unitholders' Equity		225,301	226,357
	\$	280,261	\$ 266,483

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

Subsequent event (note 10)

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

Approved by the Trustees

*"Stan Bracken-Horrocks"*

Stan Bracken-Horrocks

*"Charles Jago"*

Charles Jago



## Canfor Pulp Income Fund

### Notes to the Unaudited Interim Consolidated Financial Statements as at December 31, 2010

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

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

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

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

On January 1, 2011, the Fund was converted to a corporation named Canfor Pulp Products Inc. See subsequent event note 10.

#### 2. Significant Accounting Policies

These unaudited interim consolidated financial statements do not include all of the disclosures required by Canadian generally accepted accounting principles for annual financial statements and, accordingly, should be read in conjunction with the audited consolidated financial statements and notes included in the Fund's 2009 Annual Report available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com). These unaudited interim consolidated financial statements follow the same accounting policies and methods of computation as used in the 2009 audited consolidated financial statements.

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

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

(thousands of dollars, unaudited)	Year ended December 31, 2010	Year ended December 31, 2009
Balance, beginning of year	263,644	266,274
Equity interest in income of the Partnership	88,643	6,644
Equity interest in other comprehensive income (loss) of the Partnership	26	(45)
Distributions from the Partnership	(91,573)	(9,229)
Balance, end of year	260,740	263,644

#### 4. Distributions

The Fund declared distributions in the twelve months of 2010 as follows:

(thousands of dollars, except per unit amounts, unaudited)			
Record Date	Payable Date	Amount per Fund Unit \$	Amount \$
January 29, 2010	February 15, 2010	0.08	2,840
February 26, 2010	March 15, 2010	0.12	4,259
March 31, 2010	April 15, 2010	0.12	4,259
April 30, 2010	May 14, 2010	0.12	4,259
May 31, 2010	June 15, 2010	0.20	7,099
June 30, 2010	July 15, 2010	0.20	7,099
July 30, 2010	August 13, 2010	0.22	7,809
August 31, 2010	September 15, 2010	0.22	7,809
September 30, 2010	October 15, 2010	0.25	8,873
October 29, 2010	November 15, 2010	0.25	8,873
November 30, 2010	December 15, 2010	0.25	8,873
December 31, 2010	January 14, 2011	0.55	19,521
		2.58	91,573

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

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

#### 5. Related Party Transactions

All accounting, treasury, legal and administrative functions for the Fund are performed on its behalf, without charge, by the Partnership pursuant to a support agreement. Distributions earned from the Partnership for the three months ended December 31, 2010 were \$37.3 million of which \$17.8 million was received, with the balance of \$19.5 million receivable on December 31, 2010.

#### 6. Future Income Taxes

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

(thousands of dollars, unaudited)	Year ended December 31, 2010	Year ended December 31, 2009
Expected income tax expense at statutory tax rate of nil (2009 – nil)	-	-
Future income tax recovery on temporary differences	(1,848)	(2,422)
	(1,848)	(2,422)

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

(thousands of dollars, unaudited)	December 31, 2010	December 31, 2009
Future income tax liability:		
Equity investment in the Partnership	35,439	42,347
Expected reversal of temporary differences prior to January 1, 2011	-	(5,060)
	35,439	37,287

The future income tax liability is based on a current estimate of the balance at the beginning of 2011. The balance relates to the Fund's 49.8% ownership in the Partnership and is based on temporary differences between the accounting and tax basis of the Partnership's assets and liabilities expected to reverse after January 1, 2011.

## 7. Accumulated Other Comprehensive Income

(thousands of dollars, unaudited)	Year ended December 31, 2010	Year ended December 31, 2009
Balance, beginning of year	32	77
Other comprehensive income (loss)	26	(45)
Balance, end of year	58	32

## 8. Financial Instruments

The Fund's financial instruments consist of distributions receivable from the Partnership and distributions payable to unitholders. Distributions receivable are classified as loans and receivables, and are measured at amortized cost. Distributions payable are classified as other liabilities and are measured at amortized cost. The carrying values of these financial instruments approximate their fair values due to the relatively short period to maturity of these instruments.

The Fund is exposed to certain risks related to the nature of its investment in the Partnership and the structure of the Fund, as well as the underlying risks related to the business of the Partnership. The Fund relies on the objectives, policies and processes of the Partnership for managing these risks.

## 9. Segmented Information

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

## 10. Subsequent Event

The conversion of the Fund into a dividend paying public taxable Canadian corporation named Canfor Pulp Products Inc. has been completed effective January 1, 2011 under the previously announced plan of arrangement approved by unitholders in April 2010. Under the arrangement, unitholders of the Fund received, for each unit of the Fund held, one common share of CPPI. The conversion was completed on a tax-free rollover basis in accordance with the legislation enacted on March 12, 2009 by the Canadian government (SIFT Conversion Rules). The reorganization was completed with the winding up of the Fund and Trust.

**Canfor Pulp Limited Partnership**  
**Consolidated Statements of Income, Comprehensive Income and Partners' Equity**

(millions of dollars, except units and per unit amounts, unaudited)	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
<b>Revenue</b>				
Sales	\$ 266.1	\$ 220.2	\$ 1,001.1	\$ 813.5
Business interruption insurance	-	-	-	3.2
	<b>266.1</b>	<b>220.2</b>	<b>1,001.1</b>	<b>816.7</b>
<b>Costs and expenses</b>				
Manufacturing and product costs	169.4	158.8	622.0	611.2
Freight and other distribution costs	32.3	29.6	122.7	121.1
Amortization	11.9	12.6	47.4	49.4
Selling and administration costs	5.9	4.8	26.3	23.0
	<b>219.5</b>	<b>205.8</b>	<b>818.4</b>	<b>804.7</b>
<b>Operating income</b>	<b>46.6</b>	<b>14.4</b>	<b>182.7</b>	<b>12.0</b>
Interest expense, net	(1.9)	(2.2)	(7.8)	(10.1)
Foreign exchange gain on long-term debt	3.9	2.9	5.7	19.6
Gain (loss) on derivative financial instruments (note 11)	2.3	0.5	1.5	(1.5)
Foreign exchange loss on working capital	(2.8)	(0.5)	(4.0)	(6.7)
Other income (expense)	(0.2)	0.1	(0.1)	0.1
	<b>1.3</b>	<b>0.8</b>	<b>(4.7)</b>	<b>1.4</b>
<b>Net income</b>	<b>47.9</b>	<b>15.2</b>	<b>178.0</b>	<b>13.4</b>
Other comprehensive income (loss) (note 14)	-	-	0.1	(0.1)
<b>Comprehensive income</b>	<b>\$ 47.9</b>	<b>\$ 15.2</b>	<b>\$ 178.1</b>	<b>\$ 13.3</b>
<b>Net income per Partnership unit</b> (note 10)				
Basic and diluted	\$ 0.68	\$ 0.21	\$ 2.50	\$ 0.19
<b>Weighted average Partnership units outstanding</b>	<b>71,270,025</b>	<b>71,270,025</b>	<b>71,270,025</b>	<b>71,270,025</b>
<b>Partners' Equity</b>				
Balance, beginning of period	\$ 550.2	\$ 523.9	\$ 529.1	\$ 534.4
Net income	47.9	15.2	178.0	13.4
Distributions declared to partners (note 13)	(74.8)	(10.0)	(183.9)	(18.6)
Other comprehensive income (loss) (note 14)	-	-	0.1	(0.1)
<b>Balance, end of period</b>	<b>\$ 523.3</b>	<b>\$ 529.1</b>	<b>\$ 523.3</b>	<b>\$ 529.1</b>

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

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

	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
(millions of dollars, unaudited)				
<b>Cash and cash equivalents generated from (used in)</b>				
<b>Operating activities</b>				
Net income	\$ 47.9	\$ 15.2	\$ 178.0	\$ 13.4
Items not affecting cash:				
Amortization	11.9	12.6	47.4	49.4
Foreign exchange gain on long-term debt	(3.9)	(2.9)	(5.7)	(19.6)
Increase in value of outstanding derivative instruments (note 11)	(1.4)	(0.9)	(1.0)	(2.1)
Employee future benefits, net of cash payments	1.9	1.5	7.7	5.2
Change in long-term maintenance provision	0.8	3.6	8.4	5.9
Other	0.1	0.1	(0.2)	0.4
Salary pension plan contribution	(4.6)	(0.6)	(6.5)	(2.5)
Other deferred expenditure	-	(0.2)	-	(0.2)
Long-term maintenance expenditure	(0.3)	(7.1)	(6.1)	(10.5)
Cash flow from operations before working capital changes	52.4	21.3	222.0	39.4
Changes in non-cash working capital (note 12)	36.9	(43.8)	(2.4)	31.8
	89.3	(22.5)	219.6	71.2
<b>Financing activities</b>				
Distributions paid to partners	(53.5)	(5.0)	(150.4)	(15.7)
Operating loan repayment (note 7)	-	-	-	(25.2)
	(53.5)	(5.0)	(150.4)	(40.9)
<b>Investing activities</b>				
Property, plant and equipment, net (note 12)	(18.2)	(2.9)	(38.7)	(17.3)
Green Transformation Program reimbursements	19.1	-	20.2	-
Net insurance proceeds	-	-	-	0.1
	0.9	(2.9)	(18.5)	(17.2)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>36.7</b>	<b>(30.4)</b>	<b>50.7</b>	<b>13.1</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>27.5</b>	<b>43.9</b>	<b>13.5</b>	<b>0.4</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 64.2</b>	<b>\$ 13.5</b>	<b>\$ 64.2</b>	<b>\$ 13.5</b>

Supplementary cash flow information (note 12).

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

# **Canfor Pulp Limited Partnership** **Consolidated Balance Sheets**

(millions of dollars, unaudited)	As at December 31, 2010	As at December 31, 2009
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 64.2	\$ 13.5
Accounts receivable (note 9)		
Trade	108.0	110.5
Other	14.8	8.6
Green Transformation Program (note 15)	17.9	-
Inventories (note 3)	123.4	135.4
Prepaid expenses and other assets	21.8	18.4
Total current assets	350.1	286.4
<b>Property, plant and equipment</b> (note 4)	499.6	534.1
<b>Other long-term assets</b> (note 5)	17.6	17.1
	\$ 867.3	\$ 837.6
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 9)	\$ 139.3	\$ 134.5
Distributions payable (note 13)	39.2	5.7
Total current liabilities	178.5	140.2
<b>Long-term debt</b> (note 7)	109.4	115.1
<b>Long-term liabilities</b> (note 8)	56.1	53.2
	\$ 344.0	\$ 308.5
<b>PARTNERS' EQUITY</b> – 14,254,005 Class A Limited Partnership Units and 57,016,020 Class B Limited Partnership Units	523.3	529.1
	\$ 867.3	\$ 837.6

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

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

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

*"Stan Bracken-Horrocks"*

Stan Bracken-Horrocks  
Director

*"Joe Nemeth"*

Joe Nemeth  
Director

## Canfor Pulp Limited Partnership

### Notes to the Unaudited Interim Consolidated Financial Statements as at December 31, 2010

#### 1. Business Description and Basis of Presentation of Financial Statements

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

At December 31, 2010, Canfor owned 50.2% and Canfor Pulp Income Fund (the Fund) indirectly owned 49.8% of the issued and outstanding units of the Partnership.

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

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

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

#### *Economic Dependence*

The Partnership depends on Canfor to provide approximately 56% (2009 Year – 63%) of its fibre supply as well as to provide certain key business and administrative services as described in the Fund's 2009 Annual Report available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com). As a result of these relationships the Partnership considers its operations to be dependent on its ongoing relationship with Canfor.

#### 2. Significant Accounting Policies

These unaudited interim consolidated financial statements do not include all of the note disclosures required by Canadian generally accepted accounting principles for annual financial statements. The Partnership's accounting policies are as disclosed in the annual consolidated financial statements of the Partnership included in the Fund's 2009 Annual Report available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com). These unaudited interim consolidated financial statements follow the same accounting policies and methods of computation as used in the 2009 audited consolidated financial statements.

#### 3. Inventories

(millions of dollars, unaudited)	December 31, 2010	December 31, 2009
Pulp	52.7	55.2
Paper	10.1	15.9
Wood chips	16.4	21.5
Processing materials and supplies	44.2	42.8
	123.4	135.4

#### 4. Property, Plant and Equipment

(millions of dollars, unaudited)	December 31, 2010		
	Cost	Accumulated amortization	Net
Land and improvements	5.4	-	5.4
Asset retirement - Landfill	2.3	0.9	1.4
Buildings, machinery and equipment	1,356.1	867.0	489.1
Construction in progress	3.7	-	3.7
	<b>1,367.5</b>	<b>867.9</b>	<b>499.6</b>

(millions of dollars, unaudited)	December 31, 2009		
	Cost	Accumulated amortization	Net
Land and improvements	5.4	-	5.4
Asset retirement - Landfill	2.3	0.8	1.5
Buildings, machinery and equipment	1,344.1	820.1	524.0
Construction in progress	3.2	-	3.2
	<b>1,355.0</b>	<b>820.9</b>	<b>534.1</b>

#### 5. Other Long-term Assets

(millions of dollars, unaudited)	December 31, 2010	December 31, 2009
Pension benefit plan	14.0	11.3
Maintenance shutdown costs	3.1	5.4
Other	0.5	0.4
	<b>17.6</b>	<b>17.1</b>

#### 6. Employee Future Benefits

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

Total employee future benefit expenses were as follows:

(millions of dollars, unaudited)	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
Pension plans	1.5	1.3	6.0	5.0
Other employee future benefit plans	1.1	0.9	4.4	3.5
Contributions to forest industry union plans	1.3	1.5	6.4	6.5
	<b>3.9</b>	<b>3.7</b>	<b>16.8</b>	<b>15.0</b>

#### 7. Credit Facilities and Long-term Debt

At December 31, 2010 the Partnership has outstanding long-term debt of \$109.4 million (2009 – \$115.1 million, US\$110.0 million for both 2010 and 2009) in the form of unsecured US dollar private placement notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013.



The Partnership has a \$40 million bank credit facility with a maturity date of November 30, 2011, of which \$0.5 million was utilized at December 31, 2010 for a standby letter of credit issued for general business purposes. In addition, the Partnership has arranged a separate facility with a maturity date of November 30, 2011, to cover the \$13.2 million standby letter of credit issued to BC Hydro under the Energy Purchase Agreement. Interest and other costs of the bank credit facility are at prevailing market rates.

The Notes and bank credit agreements each contain similar financial covenants including a maximum allowable debt:EBITDA leverage ratio and minimum required EBITDA:interest coverage ratio. The Partnership remained in compliance with all covenants at December 31, 2010 and throughout the year.

The fair value of long-term debt at December 31, 2010 was \$117.8 million (US\$118.4 million).

## 8. Long-term Liabilities

(millions of dollars, unaudited)	December 31, 2010	December 31, 2009
Pension obligations under defined benefit plans	6.6	5.8
Post-employment benefits	46.2	43.2
Other pension obligations	0.2	-
Derivative financial instruments (note 11)	-	1.2
Asset retirement obligations	3.1	3.0
	<b>56.1</b>	<b>53.2</b>

## 9. Related Party Transactions

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2009 audited consolidated financial statements and are based on agreed upon amounts between the parties, and are summarized below:

(millions of dollars, unaudited)	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
<b>Transactions</b>				
Canfor	25.9	29.5	124.3	118.2
Howe Sound LP – commission received	-	0.5	1.8	2.4
Howe Sound LP – sale of wood chips	-	-	-	0.1
Howe Sound LP – contract termination fee	1.3	-	1.3	-
Lakeland Mills Ltd. – purchase of wood chips	1.8	1.2	6.1	3.9
			<b>December 31, 2010</b>	<b>December 31, 2009</b>
<b>Balance Sheet</b>				
Included in accounts payable and accrued liabilities:				
Canfor			44.5	40.8
Howe Sound LP			-	17.6
Lakeland Mills Ltd.			0.4	0.4
Included in trade accounts receivable:				
Product marketed for Canfor			23.2	24.4
Product marketed for Howe Sound LP			-	16.5

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

## 10. Net Income (Loss) per Partnership Unit

Basic net income (loss) per Partnership unit is based on the weighted average number of Limited Partnership units outstanding during the period. All outstanding Partnership units were issued on July 1, 2006, and there was no change in the number of outstanding Partnership units during the quarter.

## 11. Derivative Financial Instruments

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

For the fourth quarter of 2010 the Partnership recorded a net gain on derivative financial instruments of \$2.3 million (fourth quarter 2009 – \$0.5 million) relating to the settlement of maturing contracts during the quarter, and the revaluation to market of outstanding contracts at the end of the quarter, for natural gas swaps and US dollar forward contracts.

The Partnership recorded losses of \$1.1 million during the fourth quarter of 2010 (fourth quarter 2009 – \$1.6 million) relating to settlement of maturing natural gas contracts as a charge to non-operating income. At December 31, 2010 the Partnership had outstanding commodity swaps hedging future natural gas purchases of 0.6 million gigajoules extending to October 2011. At December 31, 2010 the unrealized loss of \$2.5 million (December 31, 2009 – \$3.5 million) on these outstanding commodity swaps was recorded as a liability in accounts payable and accrued liabilities.

The Partnership recorded a gain of \$2.0 million during the fourth quarter of 2010 (fourth quarter 2009 – \$1.2 million) on settlement of maturing US dollar forward contracts to non-operating income. At December 31, 2010 the Partnership had outstanding US dollar forward contracts of \$60.0 million extending to April 2011. At December 31, 2010 the unrealized gain of \$1.1 million (December 31, 2009 – \$1.1 million) on these outstanding US dollar forward contracts was recorded as an asset in other accounts receivable.

## 12. Supplementary Cash Flow Information

(millions of dollars, unaudited)	Three months ended		Year ended	
	December 31, 2010	December 31, 2009	December 31, 2010	December 31, 2009
<b>Decrease (increase) in non-cash working capital</b>				
Accounts receivable – trade and other	15.2	(12.3)	(3.5)	(33.4)
Insurance receivable	-	-	-	7.3
Inventories	19.7	4.5	11.9	41.3
Prepaid expenses and other assets	9.9	(4.8)	(3.4)	(1.8)
Accounts payable and accrued liabilities	(7.9)	(31.2)	(7.4)	18.4
	36.9	(43.8)	(2.4)	31.8
<b>Capital expenditures</b>				
Capital expenditures – cash	18.2	2.9	38.7	17.3
Less amount reimbursable - Green Transformation Program	(14.3)	-	(26.7)	-
	3.9	2.9	12.0	17.3
Proceeds on disposal of fixed assets	0.2	-	0.5	-
Capital expenditures accruals – net accruals	(0.3)	(0.4)	0.6	(3.8)
	3.8	2.5	13.1	13.5
<b>Net interest paid</b>	3.5	3.7	7.5	9.0

### 13. Distributions

The Partnership declared distributions in the twelve months of 2010 as follows:

(millions of dollars, except per unit amounts, unaudited)

<b>Record Date</b>	<b>Payable Date</b>	<b>Amount per Partnership Unit</b>	<b>Amount</b>
		<b>\$</b>	<b>\$</b>
January 29, 2010	February 15, 2010	0.08	<b>5.7</b>
February 26, 2010	March 15, 2010	0.12	<b>8.5</b>
March 31, 2010	April 15, 2010	0.12	<b>8.6</b>
April 30, 2010	May 14, 2010	0.12	<b>8.6</b>
May 31, 2010	June 15, 2010	0.20	<b>14.2</b>
June 30, 2010	July 15, 2010	0.20	<b>14.3</b>
July 30, 2010	August 13, 2010	0.22	<b>15.7</b>
August 31, 2010	September 15, 2010	0.22	<b>15.7</b>
September 30, 2010	October 15, 2010	0.25	<b>17.8</b>
October 29, 2010	November 15, 2010	0.25	<b>17.8</b>
November 30, 2010	December 15, 2010	0.25	<b>17.8</b>
December 31, 2010	January 14, 2011	0.55	<b>39.2</b>
		<b>2.58</b>	<b>183.9</b>

### 14. Accumulated Other Comprehensive Income

(millions of dollars, unaudited)	<b>Year ended December 31, 2010</b>	Year ended December 31, 2009
Balance, beginning of year	-	0.1
Adjustment for exchange translation	<b>0.1</b>	(0.2)
Adjustment for derivatives recorded in other comprehensive income	-	0.1
Balance, end of year	<b>0.1</b>	-

Since the inception of the Partnership, the total of the cumulative comprehensive income, less cumulative distributions is as follows:

(millions of dollars, unaudited)	<b>December 31, 2010</b>
Cumulative comprehensive income	<b>454.8</b>
Cumulative distributions	<b>(519.0)</b>
	<b>(64.2)</b>
Partners' capital – at July 1, 2006	<b>587.5</b>
Partners' equity, end of year	<b>523.3</b>

### 15. Green Transformation Program

On October 9, 2009 the Canadian Federal government announced the allocation of credits from the billion dollar Pulp and Paper Green Transformation Program (the Program). The Partnership has been allocated \$122.2 million from the Program announced by the Canadian government on June 17, 2009. The Program is designed as a reimbursement of funds to be spent on qualifying energy and environmental capital projects. Credits may be used until the program end date of March 31, 2012. The Partnership has received Program approval to proceed with three projects totaling \$115.6 million. The Partnership expects to submit further projects over the balance of 2011. As of December 31, 2010 the Partnership has incurred \$38.1 million and received reimbursements totaling \$20.2 million with the balance of \$17.9 million receivable on December 31, 2010. The Partnership submits claims for expenditures

on approved projects under the Program on a monthly basis. These projects are expected to provide economic and environmental benefits to the Partnership's operations.

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

(millions of dollars, unaudited)	Pulp	Paper	Unallocated Costs	Total
<b>Three months ended December 31, 2010</b>				
Sales to external customers <sup>(b)</sup>	224.7	40.9	0.5	266.1
Sales of pulp to paper segment <sup>(c)</sup>	22.8	(22.8)	-	-
Operating income	47.4	1.4	(2.2)	46.6
Amortization	11.1	0.7	0.1	11.9
Capital expenditures, net	3.3	0.3	0.2	3.8
Three months ended December 31, 2009				
Sales to external customers <sup>(b)</sup>	186.9	32.3	1.0	220.2
Sales of pulp to paper segment <sup>(c)</sup>	20.9	(20.9)	-	-
Operating income	17.9	0.1	(3.6)	14.4
Amortization	11.8	0.8	-	12.6
Capital expenditures, net	2.3	0.1	0.1	2.5
<b>Year ended December 31, 2010</b>				
Sales to external customers <sup>(b)</sup>	857.2	142.6	1.3	1,001.1
Sales of pulp to paper segment <sup>(c)</sup>	89.6	(89.6)	-	-
Operating income	198.1	0.5	(15.9)	182.7
Amortization	44.1	3.0	0.3	47.4
Capital expenditures, net	10.9	1.3	0.9	13.1
Identifiable assets	707.5	63.7	96.1	867.3
Year ended December 31, 2009				
Sales to external customers <sup>(b)</sup>	690.0	122.5	1.0	813.5
Sales of pulp to paper segment <sup>(c)</sup>	63.7	(63.7)	-	-
Operating income	11.7	10.6	(10.3)	12.0
Amortization	45.9	3.3	0.2	49.4
Capital expenditures, net	13.2	0.1	0.2	13.5
Identifiable assets	739.3	64.4	33.9	837.6

(a) Operations are presented by product lines. Operations are considered to be in one geographic area since all production facilities are in Canada. Substantially all sales are exported outside Canada, with sales to the United States representing 37% (2009 – 36%).

(b) Sales to the largest customer represented approximately 12% of pulp segment sales (2009 – 9%).

(c) Sales of slush pulp to the paper segment are accounted for at approximate market value. The sales are transacted as a cost transfer and are not reflected in Pulp sales.