

# CANFOR PULP INCOME FUND

## First Quarter Report

For the three months ended March 31, 2009

**Canfor Pulp Income Fund and Canfor Pulp Limited Partnership  
First Quarter 2009  
Management's Discussion and Analysis**

*Canfor Pulp Income Fund (the Fund) earns income from its 49.8% indirect interest in Canfor Pulp Limited Partnership (the Partnership). The Fund accounts for its investment in the Partnership on the equity basis and does not consolidate the operations of the Partnership. In order for the Fund's unitholders to understand the results of operations, the unaudited interim consolidated financial statements with accompanying notes are presented for both the Fund and the Partnership. This Management's Discussion and Analysis (MD&A) provides a review of the significant developments that have impacted the Partnership's and the Fund's performance for the quarter ended March 31, 2009 relative to the same period in the prior year and relative to the previous quarter. This MD&A should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes as well as the annual MD&A and audited consolidated financial statements and notes which are included in the Fund's 2008 Annual Report. Additional information relating to the Fund and the Partnership, including the Fund's Annual Information Form (AIF) dated February 17, 2009, is available on SEDAR at [www.sedar.com](http://www.sedar.com) or at [www.canforpulp.com](http://www.canforpulp.com).*

*Factors that could impact future operations are also discussed. These factors may be influenced by known and unknown risks and uncertainties that could cause the actual results to be materially different from those stated in this discussion. Factors that could have a material impact on any future oriented statements made herein include, but are not limited to: 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 Partnership.*

*In this document, references are made to EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization and before other non-operating income and expenses) and adjusted distributable cash. The Partnership considers EBITDA to be an important indicator for identifying trends in the Partnership's performance and of the Partnership's ability to generate funds to meet its debt service, capital expenditure requirements and to make cash distributions to its partners. Adjusted distributable cash is a measure of cash flow used by management to determine the level of cash distributions. EBITDA and adjusted distributable cash should not be considered as alternatives to net income or cash flow from operations as determined in accordance with Canadian generally accepted accounting principles. As there is no standardized method of calculating EBITDA, the Partnership's use of this term may not be directly comparable with similarly titled measures used by other companies or income funds.*

*Calculations of EBITDA and adjusted distributable cash are provided in a schedule at the end of this MD&A.*

*The information in this report is as at April 27, 2009.*

**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. The risks and uncertainties are detailed from time to time in reports filed by the Fund with the securities regulatory authorities in all of the provinces and territories of Canada to which recipients of this press release are referred to for additional information concerning the Fund and Partnership, its prospects and uncertainties relating to the Fund and Partnership and its prospects. These 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 results, performance and achievements of the Fund and Partnership to be materially different from those contained in forward-looking statements. The forward-looking statements are based on current information and expectations and the Fund and 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;*
- *“Conversion to International Financial Reporting Standards” on pages 4 and 5;*
- *“Outlook – Pulp” on page 9;*
- *“Outlook – Kraft Paper” on page 10;*
- *“Liquidity and Financial Requirements” on page 12;*
- *“Critical Accounting Estimates” on page 13;*
- *“Conversion to International Financial Reporting Standards” on page 14;*
- *“Distributable Cash and Cash Distributions” on page 15.*

*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 Partnership. Additional information concerning these and other factors can be found in the Fund’s Annual Information Form dated February 17, 2009, which is available on [www.sedar.com](http://www.sedar.com).*

## 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 Limited Partnership Units of 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 limited partner holds an ownership interest in the General Partner equal to its proportionate interest in the Partnership.

At April 27, 2009, there were a total of 35,493,505 Fund units issued and outstanding, and the Fund indirectly held a total of 35,493,542 units of the Partnership, representing 49.8% of the Partnership and Canfor held 35,776,483 Class B Exchangeable Limited Partnership Units, representing 50.2% of the Partnership. The Class B Exchangeable LP Units are indirectly exchangeable for an equivalent number of Fund Units pursuant to the terms of an exchange agreement (Exchange Agreement) dated July 1, 2006 among Canadian Forest Products Ltd. (CFP), the Fund, Canfor Pulp Trust, Canfor Pulp Limited Partnership and Canfor Pulp Holding Inc. The Exchange Agreement contains, among other things, the procedure through which the Class B Exchangeable LP Units may be exchanged for Fund Units.

Each unitholder participates pro-rata in any distributions from the Fund. Under present income tax legislation, income tax obligations related to the distributions of the Fund are the obligations of the unitholders and the Fund is only taxable on any amount not allocated to the unitholders.

### SELECTED QUARTERLY FUND FINANCIAL INFORMATION

(thousands of dollars, except per unit amounts, unaudited)	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007
Equity income (loss) in Canfor Pulp Limited Partnership	<b>(10,740)</b>	(12,947)	5,513	9,046	21,667	5,999	16,541	17,900
Net income (loss) <sup>1</sup>	<b>(10,740)</b>	(13,686)	5,208	7,015	21,667	8,703	16,541	(21,437)
Net income (loss) per Fund unit <sup>1</sup>	<b>\$(0.30)</b>	\$(0.39)	\$0.15	\$0.20	\$0.61	\$0.25	\$0.46	\$(0.60)
Distributions earned from the Partnership and declared to unitholders	<b>2,130</b>	9,938	12,778	12,777	12,778	13,487	19,167	17,747
Distributions declared per Fund unit	<b>\$0.06</b>	\$0.28	\$0.36	\$0.36	\$0.36	\$0.38	\$0.54	\$0.50

Note: <sup>1</sup> In the second quarter of 2007 the Fund recorded a non-cash future income tax charge of \$39.3 million to net income relating to the Fund's 49.8% ownership in the Partnership and based on temporary differences between the accounting and tax basis of the Partnership's assets and liabilities expected to reverse after January 1, 2011.

### OPERATING RESULTS AND LIQUIDITY

For the quarter ended March 31, 2009, the Fund had a net loss of \$10.7 million or \$0.30 per Fund unit. The net loss is the Fund's share of the Partnership's loss for the first quarter of 2009. The Fund's equity loss in the Partnership is \$2.2 million less than the prior quarter due to the Fund's share of the Partnership's higher operating loss, which was more than offset by a reduction in losses of non-operating items. The Fund's share of operating loss increased by \$4.4 million due primarily to lower prices for the Partnership's pulp and paper products. Non-operating items for the first quarter of 2009 totaled \$5.9 million compared to \$12.5 million in the fourth quarter 2008 with the reduction mainly the result of a lower foreign exchange loss on translation of US dollar denominated long-term debt, and lower losses on settlement and revaluation to market of derivative financial instruments. Distributions declared by the Partnership and accruing to the Fund were \$2.1 million of which \$0.3 million was receivable at March 31, 2009. Cash distributions received from the Partnership are the only source of liquidity for the Fund. The Fund's requirements for administrative services are minimal and are funded and expensed by the Partnership. For further information refer to the Partnership's discussion of operating results and liquidity on pages 8 through 13 of this press release.

## **FUND DISTRIBUTIONS**

The Fund is entirely dependent on distributions from the Partnership to make its own distributions and declares 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 are recorded when declared. During the first quarter of 2009, the Fund declared distributions of \$0.06 per Fund unit or \$2.1 million.

Monthly cash distributions from the Partnership are not directly equal to the Fund's pro-rata share of the Partnership's income (loss) under the equity method, 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 is 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 17, 2009, which is available on [www.sedar.com](http://www.sedar.com) and [www.canforpulp.com](http://www.canforpulp.com).

## **FUND UNITS**

At April 27, 2009, there were a total of 35,493,505 Fund units outstanding.

## **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 March 31, 2009 were \$2.1 million of which \$1.8 million was received, with the balance of \$0.3 million receivable on March 31, 2009.

## **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 accounts for its investment in the Partnership using the equity method. Management periodically evaluates whether there has been an other than temporary decline in the value of the investment in the Partnership. The Fund relies on the recoverability analysis of the Partnership for the purposes of this assessment. Changes in these estimates could have a material impact on the calculation of the future income tax liability or equity investment in the Partnership.

## **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. The Fund will rely on the resources of the Partnership to ensure compliance with IFRS. The Partnership intends to convert to these new standards according to the timetable set for these new rules and has completed the following steps:

- Commenced a comprehensive Institute of Chartered Accountants of BC in-house training program for the Partnership's Finance team. This program has included an overview of IFRS and was tailored to issues that may impact the financial statements, disclosures and results of operations of the Fund and Partnership.

- Formally established a transition plan, steering committee and a project implementation team. The project team consists of members from Finance and Information Technology and is being overseen by the Partnership's Chief Financial Officer. Reporting is done to senior management and to the Audit Committee on a regular basis.
- Completed the first phase of its transition program, which included scoping to identify the significant accounting policy differences and their related areas of impact in terms of systems, procedures and financial statements.
- Commenced the second phase of the transition plan, which involves a completed design and work plan to measure the differences between IFRS and Canadian GAAP, and the impact on its financial statements, disclosures and results of operations.

The Fund expects the transition to IFRS to impact financial reporting, business processes and information systems of the Partnership, which the Fund relies on. The Partnership will continue to review all proposed and continuing projects of the International Accounting Standards Board to determine their impact on the Fund, and will continue to invest in training and resources throughout the transition period to facilitate a timely conversion.

At this time, the impact on the Fund's future financial position and results of operations is not reasonably determinable.

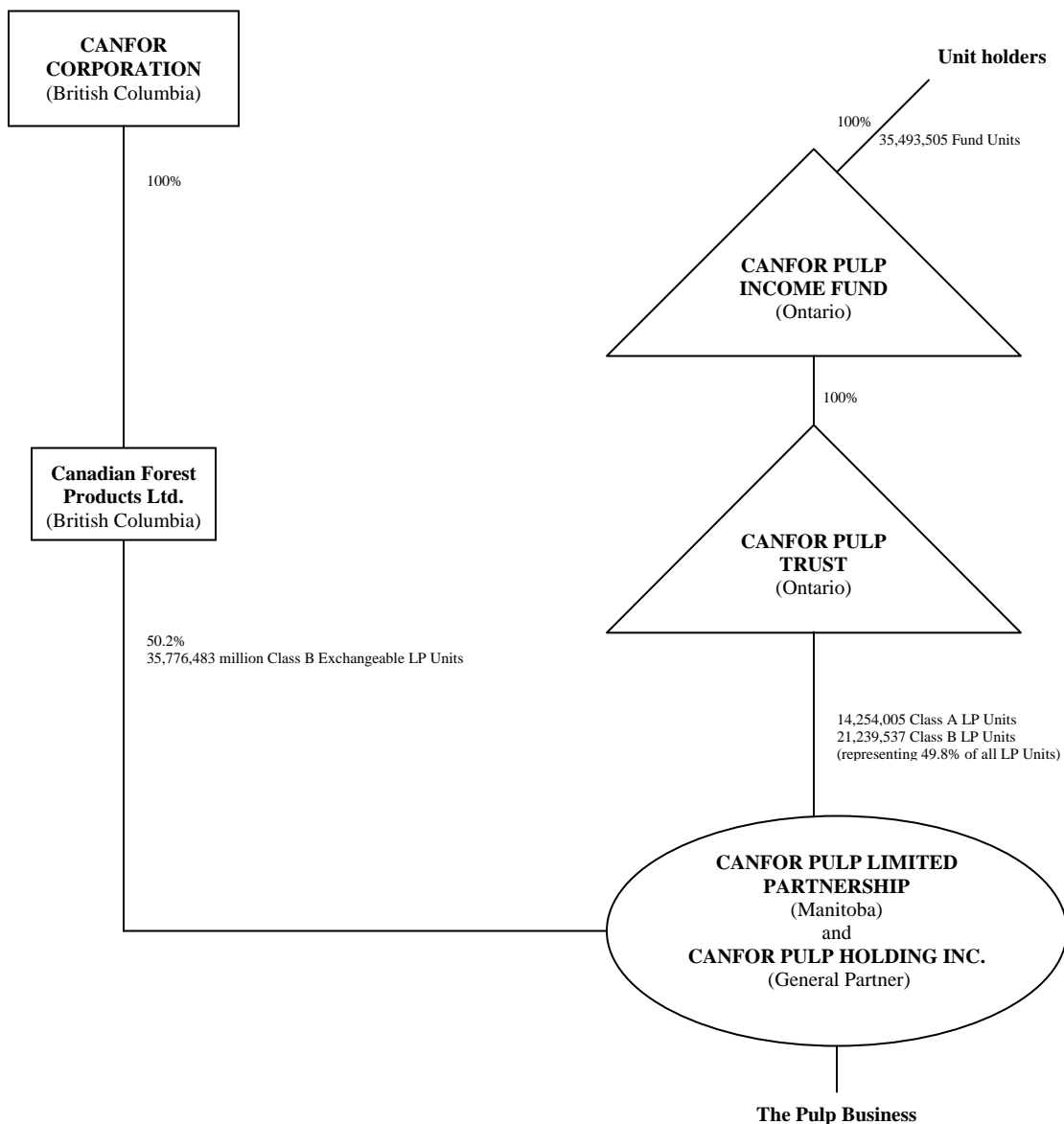
## CANFOR PULP LIMITED PARTNERSHIP

### Structure

The Partnership is a limited partnership formed on April 21, 2006, under the laws of Manitoba to acquire and carry on the 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).

At April 27, 2009, the Fund 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. Below is a simplified schematic of the ownership structure.

### Partnership Structure



## 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>Q1 2009</b>	Q4 2008	Q1 2008
Sales	<b>186.3</b>	186.1	211.4
EBITDA <sup>1</sup>	<b>2.2</b>	9.8	42.5
Operating income (loss)	<b>(9.8)</b>	(1.0)	30.6
Net income (loss)	<b>(21.6)</b>	(26.0)	43.5
Per Partnership unit, basic and diluted			
Net income (loss)	<b>(0.30)</b>	(0.36)	0.61
EBITDA	<b>0.03</b>	0.14	0.60
Average exchange rate (US\$/Cdn\$) <sup>2</sup>	<b>0.803</b>	0.825	0.996

Notes: <sup>1</sup> For calculation of EBITDA, see supplementary financial information on page 15.

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

EBITDA for the first quarter of 2009 decreased by \$7.6 million from the fourth quarter of 2008 and was \$40.3 million lower when compared to the first quarter of 2008. Financial results of the Partnership continue to be significantly impacted by the global financial crisis resulting in a reduction in global demand for pulp and paper products, increased global inventory levels, and further reductions in NBSK pulp list prices. As a result of these adverse conditions the Partnership commenced a market curtailment in December 2008 that continued into 2009. The market curtailment allowed the Partnership to manage inventory levels and to mitigate the impact of the significant reductions in global demand heading into the 2009 year. The decrease in first quarter 2009 EBITDA, when compared to the fourth quarter of 2008, is primarily related to a 15% decrease in NBSK pulp US dollar list price. The lower list prices were partially offset by a weaker Canadian dollar, and lower unit manufacturing and freight costs. Lower unit manufacturing costs were the result of higher production volumes, lower spending on fixed costs and lower fibre costs. Lower spending on fixed costs in the first quarter of 2009, compared to the prior quarter, was primarily attributable to a reduction in scheduled maintenance outages. Fibre costs decreased by approximately 9% due to lower prices for sawmill residual chips and the cessation of several high cost whole log chipping initiatives. Freight costs in US dollar terms were 7% lower when compared to the fourth quarter of 2008 as a result of a higher percentage of sales into Asia and an overall trend downwards in rates and fuel surcharges. The 15% decline in NBSK pulp US dollar list price was partially offset by a 3% weakening of the Canadian dollar.

When compared to the first quarter of 2008, the \$40.3 million decrease in EBITDA was primarily attributable to lower NBSK pulp US dollar list prices, reduced production volumes and higher freight costs, partially offset by lower fibre costs, a weaker Canadian dollar and higher sales volumes. NBSK pulp US dollar list price decreased 24% when compared to the same period a year ago and increases in the Partnership's sales into lower margin business consisting primarily of the tissue segment and non-contract business were partially offset by the significantly weaker Canadian dollar. Fibre costs decreased approximately 5% due to lower prices for sawmill residual and whole log chips. First quarter 2009 production was lower by approximately 36,000 tonnes when compared to the same period in 2008 after accounting for the impact of the fire at the Prince George Pulp and Paper Mill in January 2008. The fire was covered by business interruption insurance which totalled \$11.4 million in the first quarter of 2008. The first quarter 2009 production was impacted by a market curtailment and maintenance outage. Overall freight costs increased by 13% in Canadian dollar terms as a 19% weaker Canadian dollar was partially offset by lower container



rates and fuel surcharges. Realized paper prices in Canadian dollar terms increased by 8% when compared to the first quarter of 2008.

## OPERATING RESULTS BY BUSINESS SEGMENT

### Pulp

(millions of dollars unless otherwise noted, unaudited)	<b>Q1 2009</b>	Q4 2008	Q1 2008
Sales <sup>1</sup>	<b>159.2</b>	159.1	176.2
EBITDA (loss)	<b>(0.5)</b>	9.5	44.0
EBITDA (loss) margin	<b>0%</b>	6%	25%
Operating income (loss)	<b>(11.6)</b>	(0.4)	33.0
Average NBSK pulp list price – (US\$ per tonne, delivered to USA)	<b>673</b>	787	880
Average NBSK pulp list price – (Cdn\$ per tonne, delivered to USA)	<b>838</b>	954	884
Production – pulp (000 mt)	<b>230.4</b>	219.6	231.5
Shipments – Partnership-produced pulp (000 mt)	<b>240.3</b>	208.2	228.9
<i>Marketed on behalf of HSLP &amp; Canfor (000 mt)</i>	<b>107.2</b>	79.9	128.4

Note: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

First quarter 2009 operating income of the pulp segment was \$11.2 million lower than the fourth quarter of 2008. The decrease is primarily due to lower NBSK pulp US dollar list prices, partially offset by a weaker Canadian dollar, higher production volume resulting in lower unit manufacturing costs, and lower fibre costs. NBSK pulp US dollar list price decreased 15% and was partially offset by a 3% weakening of the Canadian dollar. Lower unit manufacturing costs were the result of higher production volumes, lower spending on fixed costs and lower fibre costs. Production volumes were higher due to less downtime taken for market curtailment and maintenance outages, partially offset by lower overall operating rates which were attributable to the impact of cold weather. Lower spending on fixed costs in the first quarter of 2009, as compared to the prior quarter, were primarily attributable to reduced scheduled maintenance outages. Fibre costs decreased approximately 9% due to lower prices for sawmill residual chips and the cessation of several high cost whole log chipping initiatives. Sales volume in the first quarter of 2009 was 32,100 tonnes higher than the prior quarter as the Partnership aggressively pursued the tissue segment and non-contract spot sales. Although this business to the Partnership is at historically lower margins, the higher sales volumes mitigated the significant reduction in global demand, allowing the Partnership to reduce finished goods inventory to manageable levels.

The first quarter 2009 operating income was \$44.6 million lower than the same period a year ago. The decrease in income was the result of lower NBSK pulp US dollar list prices and the impacts of reduced production on unit manufacturing costs, partially offset by lower fibre costs, a weaker Canadian dollar and higher sales volumes. A 24% decrease in NBSK pulp US dollar list price and increases in the Partnership's sales into lower margin businesses were partially offset by a 19% weakening of the Canadian dollar, resulting in a decrease of realized prices in Canadian dollar terms of 14%. First quarter 2009 production was lower by approximately 36,000 tonnes when compared to the same period in 2008 after accounting for the impact of the fire at the Prince George Pulp and Paper Mill in January 2008. The fire was covered by business interruption insurance which totalled \$11.4 million in the first quarter of 2008. The lower production in the first quarter of 2009 was due to a market curtailment, maintenance outage and lower overall operating rates. Higher unit manufacturing costs were attributable to lower production volumes, higher spending on fixed costs due to the maintenance outage, partially offset by lower fibre costs. Fibre costs decreased approximately 5% due to lower prices for sawmill residual and whole log chips.

### Operations

NBSK market pulp production during the first quarter of 2009 was 10,800 tonnes higher than the fourth quarter of 2008. The major components of increased production in the first quarter of 2009 were decreased scheduled maintenance outages totaling 7,100 tonnes (fourth quarter 2008 – 15,900 tonnes), a decrease in market related

curtailments totaling 14,000 tonnes (fourth quarter 2008 – 25,800 tonnes), partially offset by lower overall operating rates attributable to cold weather and start-up issues coming out of the market curtailment.

When compared to the same period in 2008, first quarter 2009 production of 230,400 tonnes was 1,100 tonnes lower. However, after accounting for the impact of the January 2008 fire at the Prince George Pulp and Paper Mill (approximately 35,000 tonnes), production was 36,100 tonnes lower when compared to the first quarter of 2008. The major components of reduced production in the first quarter of 2009 were increased scheduled maintenance outages totaling 7,100 tonnes (first quarter 2008 – nil), market related curtailments totaling 14,000 tonnes (first quarter 2008 – nil), and overall lower operating rates attributable to cold weather and start-up issues coming out of the market curtailment.

#### *Markets – Pulp*

The global pulp market deteriorated further during the first quarter of 2009 resulting in lower global demand for pulp and paper products, reduced global shipments, higher producer inventories and continued pressure on prices.

The demand for market pulp has fallen largely due to reduced demand for printing and writing papers. According to the PPPC<sup>1</sup>, global demand for printing and writing papers decreased 18% for March 2009 year-to-date, when compared to the same period in 2008.

For March year-to-date 2009, the World 20<sup>1</sup> producers reported a shipment-to-capacity ratio of 84% (March 2008 – 92%) for northern bleached softwood kraft (NBSK) market pulp (per PPPC<sup>1</sup>). The World 20<sup>1</sup> NBSK market pulp shipments were down 18% year-to-date through March 2009 compared to the same period in 2008.

Pulp inventories are at high levels, by historic standards. At the end of March 2009, producer softwood pulp inventories were at 40 days of supply (March 2008 – 33 days), after peaking at 43 days in January 2009.

The price of market pulp has fallen with demand. In March of 2009, the price for NBSK settled in the USA and Europe at US\$650 per tonne and US\$580 per tonne respectively. In comparison, in December of 2008, prices were at US\$735 per tonne and US\$635 per tonne, for USA and Europe respectively and in March of 2008, both markets were priced at US\$880 per tonne.

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 (PPPC)

#### *Outlook – Pulp*

It is difficult to forecast market conditions for the balance of this year, because the supply and demand conditions in the market are changing rapidly. The lower demand and prices experienced recently have caused numerous pulp mills in Canada and Scandinavia to curtail production in order to conserve cash and control inventories. These curtailments include temporary and permanent closures. Hence the supply of market pulp is unpredictable, both short and medium-term. Demand is expected to remain under pressure in the short-term and potentially through the balance of this year. The balance of supply, demand, and the level of customer inventories are currently allowing for some very modest price gains in Asian markets. However, a recent development in the United States allows certain pulp producers to receive tax credits by defining kraft black liquor as an “alternative fuel”. This has the potential to significantly reduce cost structures of these producers.

## Paper

(millions of dollars unless otherwise noted, unaudited)	Q1 2009	Q4 2008	Q1 2008
Sales <sup>1</sup>	27.1	27.0	35.2
EBITDA	4.6	3.3	2.3
EBITDA margin	17%	12%	7%
Operating income	3.8	2.5	1.4
Production – paper (000 mt)	28.4	30.1	32.4
Shipments – paper (000 mt)	25.2	24.4	35.1

Note: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

Operating income of the paper segment for the first quarter of 2009 was \$1.3 million higher than the fourth quarter of 2008 and \$2.4 million higher than the same period last year. The increase when compared to the fourth quarter of 2008 was primarily attributable to lower unit manufacturing costs, partially offset by lower realized prices in Canadian dollar terms and lower production volumes. Lower unit manufacturing costs are the result of lower costs for slush pulp and lower spending on fixed costs, partially offset by the impact of lower production volumes. Coinciding with the market curtailment of pulp production, the Partnership completed a curtailment of paper production in January 2009, reducing paper production by approximately 4,800 tonnes in the first 12.5 days of 2009 as compared to 3,400 tonnes in 2008. Realized prices in Canadian dollar terms decreased by approximately 3%.

When compared to the first quarter of 2008 the improved operating earnings were due to an 8% increase in realized prices in Canadian dollar terms and lower unit manufacturing costs, partially offset by lower sales and production volumes. Lower unit manufacturing costs are the result of lower costs for slush pulp and lower spending on fixed costs, partially offset by the impact of lower production volumes. Lower sales volumes are the result of weak global demand for kraft paper.

### Operations

Paper production in the first quarter of 2009 decreased 1,700 tonnes when compared to the fourth quarter of 2008, and was 4,000 tonnes lower than the first quarter of 2008. Reduced production volumes in the first quarter were the result of the completion of the market curtailment that commenced in December 2008, representing 12.5 days of lost production in the first quarter of 2009 compared to nine days in the fourth quarter of 2008.

### Markets - Paper

Weak sack kraft paper demand in the fourth quarter of 2008 continued into the first quarter of 2009. The weak demand is due to the continued turmoil and general economic weakness precipitated by the global financial crisis, resulting in inventory corrections by key contract customers. Kraft paper prices slipped further in the first quarter of 2009. The decline since the price peak in the summer of 2008 has been approximately 10% with lower list prices for sack kraft paper partially offset by a weaker Canadian dollar.

The Partnership's first quarter of 2009 total prime paper shipments were down 28% from the first quarter of 2008. The Partnership's first quarter 2009 bleached shipments were down 47% from the same period in 2008.

American Forest and Paper Association reported that US total kraft paper shipments in March 2009 decreased by 3% compared to February 2009. Bleached shipments increased 1% in March 2009 compared to February 2009, but decreased 31% when compared to March 2008. Bleached inventory dropped 8% in March 2009 compared to February 2009.

### Outlook – Kraft Paper

Prices may continue to decline modestly in both domestic and offshore markets through the second quarter due to continued weak demand.

## Non-Segmented Costs

(millions of dollars, unaudited)	Q1 2009	Q4 2008	Q1 2008
Unallocated costs	2.0	3.1	3.8
Interest expense, net	2.6	2.6	1.7
Foreign exchange loss on long-term debt	3.9	18.1	3.3
Loss (gain) on derivative financial instruments	5.7	11.1	(6.9)
Foreign exchange gain on working capital	(0.6)	(7.0)	(2.6)
Net property damage insurance gain <sup>1</sup>	-	0.3	(8.5)
Other (income) expense	0.2	(0.1)	0.1
	<b>13.8</b>	28.1	(9.1)

Note: <sup>1</sup> An adjustment of \$0.3 million in the fourth quarter of 2008 reflects management's current estimate of final costs to complete the new chip screening system.

### *Unallocated Costs*

Unallocated costs, comprised principally of general and administrative expenses, totalled \$2.0 million in the first quarter of 2009 compared to \$3.1 million in the fourth quarter of 2008 and \$3.8 million in the first quarter of 2008. The reduction in unallocated costs when compared to prior periods is due to the cessation of accruals for Canfor Pulp Salaried Incentive Plans (PSIP). PSIP requires a minimum threshold of profitability prior to any payout. Management reviews the Partnership's financial performance on an ongoing basis and adjusts the PSIP accruals accordingly.

### *Interest Expense*

The increased net interest expense in the first quarter of 2009 compared to the first quarter of 2008 is due to the cost of funding short-term working capital requirements.

### *Other Non-segmented Items*

The loss on derivative financial instruments recorded in the first quarter of 2009 of \$5.7 million relates 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 foreign exchange hedging contracts. The declining price of natural gas in the first quarter of 2009 resulted in a loss for the quarter of \$1.4 million on settlement of contracts. The natural gas swaps are used to fix the price on a portion of the Partnership's future natural gas requirements. The declining value of the Canadian dollar in the first quarter of 2009 resulted in a loss for the quarter of \$1.4 million on settlement of US dollar foreign exchange contracts to hedge the impact of currency fluctuations on US dollar working capital. This loss was partially offset by the foreign exchange gain on working capital of \$0.6 million. The revaluation to market of outstanding derivative instruments recorded in the quarter of \$2.9 million relates to a revaluation to market of outstanding natural gas swaps and outstanding US dollar foreign exchange hedging contracts at the end of the quarter. This is the result of a decrease in the market price of natural gas and the weaker Canadian dollar at the end of the quarter.

The foreign exchange loss on long-term debt results from translating the US\$110 million debt at period-end exchange rates.

## 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)	Q1 2009	Q1 2008
Ratio of current assets to current liabilities	1.81	1.97
Ratio of net debt to partners' equity <sup>1</sup>	0.30	0.15
Increase in cash and cash equivalents	1.6	20.3
Comprised of cash flow from (used in):		
Operating activities <sup>2</sup>	21.8	51.6
Financing activities	(14.0)	(25.6)
Investing activities <sup>2</sup>	(6.2)	(5.7)

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

<sup>2</sup> Comparative figures have been reclassified to conform to current year presentation.

### Changes in Financial Position

Cash generated from operating activities was \$21.8 million in the first quarter of 2009 compared to \$51.6 million in the first quarter of 2008. The decrease was primarily due to lower cash generated from operations partially offset by a decrease in cash used in working capital. The lower cash generated from operations is attributable to significant reductions in the price for the Partnership's pulp and paper products, and the impact of a market curtailment at all of the Partnership's manufacturing facilities taken to manage inventory levels as a result of reduced global demand. The decrease in cash used in working capital is primarily due to reductions in cost and volume of finished goods and chip inventories and receipt of amounts in relation to the Prince George Pulp and Paper Mill fire insurance claim.

The cash used in financing activities of \$14.0 million in the quarter represents \$6.4 million of distributions paid to the limited partners, namely Canfor and the Fund, and a reduction of \$7.6 million in utilization of the Partnership's Revolving Facility.

The cash used in investing activities in the quarter is comprised of \$6.0 million relating to capital expenditures.

### LIQUIDITY AND FINANCIAL REQUIREMENTS

At the end of the current quarter, the Partnership had cash and cash equivalents of \$2.0 million. The Partnership has a \$75 million syndicated unsecured revolving bank credit facility (the Revolving Facility), maturing in November 2009, of which \$32.7 million is available, with \$24.7 million of the Revolving Facility reserved for standby letters of credit issued to BC Hydro and \$17.6 million drawn to fund working capital requirements as of March 31, 2009. The Partnership expects to renew the Revolving Facility for a similar amount, with terms and interest rates based on prevailing market conditions at the time of renewal.

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, and use of the Revolving 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 amounts periodically to manage cash resources.

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

### OUTSTANDING UNITS

At April 27, 2009, 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) are owned by the Fund through Canfor Pulp Trust and 35,776,483 Class B Exchangeable Limited Partnership Units are owned indirectly by Canfor.

## RELATED PARTY TRANSACTIONS

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2008 audited consolidated financial statements and are based on agreed upon amounts, and are summarized in note 10 of the unaudited interim consolidated financial statements.

## INTERNAL CONTROLS OVER FINANCIAL REPORTING

During the quarter ending March 31, 2009, 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 17, 2009, which is available on [www.sedar.com](http://www.sedar.com) and [www.canforpulp.com](http://www.canforpulp.com).

## SELECTED QUARTERLY PARTNERSHIP FINANCIAL INFORMATION

(unaudited)	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007
<b>Sales and Income</b> (millions of dollars)								
Sales	<b>186.3</b>	186.1	215.4	212.6	211.4	215.1	228.9	239.4
Operating income (loss)	<b>(9.8)</b>	(1.0)	27.5	11.6	30.6	11.7	35.4	39.2
EBITDA	<b>2.2</b>	9.8	40.6	24.0	42.5	27.9	48.8	51.7
Net income (loss)	<b>(21.6)</b>	(26.0)	11.1	18.2	43.5	12.1	33.2	35.9
<b>Per Partnership unit</b> (dollars) <sup>1</sup>								
Net income (loss) basic and diluted	<b>(0.30)</b>	(0.36)	0.15	0.26	0.61	0.17	0.46	0.51
<b>Statistics</b>								
Pulp shipments (000 mt)	<b>240.3</b>	208.2	234.5	233.8	228.9	253.6	257.1	259.8
Paper shipments (000 mt)	<b>25.2</b>	24.4	31.6	33.7	35.1	32.4	30.8	35.9
Average exchange rate (US\$/Cdn\$) <sup>2</sup>								
	<b>0.803</b>	0.825	0.960	0.990	0.996	1.019	0.957	0.911
Average NBSK pulp list price – (US\$ per tonne, delivered to USA)								
	<b>673</b>	787	880	880	880	857	837	810

Notes: <sup>1</sup> Based on Partnership units outstanding at March 31, 2009 (71,270,025) for all periods.

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

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 and fluctuations of fibre, chemicals 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 the Canadian dollar exchange rate, 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 commodity swaps and US dollar forward sales 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, asset retirement obligations, and provisions for insurance claims, 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**

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 intends to convert to these new standards according to the timetable set for these new rules and has completed the following steps:

- Commenced a comprehensive Institute of Chartered Accountants of BC in-house training program for the Partnership's Finance team. The program to date has included an overview of IFRS and was tailored to issues that may impact the financial statements, disclosures and results of operations of the Partnership.
- Formally established a transition plan, steering committee and a project implementation team. The project team consists of members from Finance and Information Technology and is being overseen by the Partnership's Chief Financial Officer. Reporting is done to senior management and to the Audit Committee on a regular basis.
- Completed the first phase of its transition program, which included scoping to identify the significant accounting policy differences and their related areas of impact in terms of systems, procedures and financial statements.
- Commenced the second phase of the transition plan, which involves a completed design and work plan to measure the differences between IFRS and Canadian GAAP, and the impact on its financial statements, disclosures and results of operations.

The Partnership expects the transition to IFRS to impact financial reporting, business processes and information systems. The Partnership will continue to review all proposed and continuing projects of the International Accounting Standards Board to determine their impact, and will continue to invest in training and resources throughout the transition period to facilitate a timely conversion.

At this time, the impact on the Partnership's future financial position and results of operations is not reasonably determinable.

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

(millions of dollars, unaudited)	Three months ended	
	March 31, 2009	March 31, 2008
<b>RECONCILIATION OF NET INCOME TO EBITDA</b>		
<b>Net Income (loss)</b>	\$ (21.6)	\$ 43.5
Add (deduct):		
Amortization	12.0	11.6
Net interest expense	2.6	1.7
Foreign exchange loss on long-term debt	3.9	3.3
Loss (gain) on derivative financial instruments	5.7	(6.9)
Foreign exchange gain on working capital	(0.6)	(2.6)
Loss on disposal of fixed assets	-	0.2
Net property damage insurance gain	-	(8.5)
Other expense	0.2	0.2
<b>EBITDA</b>	<b>\$ 2.2</b>	<b>\$ 42.5</b>
<b>EBITDA per Partnership unit</b>	<b>\$ 0.03</b>	<b>\$ 0.60</b>

(millions of dollars, unaudited)	Three months ended	
	March 31, 2009	March 31, 2008
<b>CALCULATION OF STANDARDIZED AND ADJUSTED DISTRIBUTABLE CASH</b>		
<b>Cash flow from operating activities</b> <sup>1</sup>	\$ 21.8	\$ 51.6
Deduct: Capital expenditures – cash	(6.0)	(9.3)
<b>Standardized distributable cash</b> <sup>1</sup>	<b>\$ 15.8</b>	<b>\$ 42.3</b>
<b>Adjustments to standardized distributable cash:</b>		
Add (deduct):		
Decrease in non-cash working capital <sup>1</sup>	(22.8)	(5.5)
Net long-term deferred maintenance	(0.9)	(1.0)
Capital expenditures - accruals	3.6	6.1
Asset retirement obligation – current expenditures and accruals <sup>1</sup>	-	0.5
<b>Adjusted distributable cash (deficiency)</b>	<b>\$ (4.3)</b>	<b>\$ 42.4</b>
Standardized distributable cash – per Partnership unit (in dollars) <sup>1</sup>	\$ 0.22	\$ 0.59
Adjusted distributable cash (deficiency)– per Partnership unit (in dollars)	\$ (0.06)	\$ 0.60
<b>Cash distributions declared (paid and payable)</b>	<b>\$ 4.3</b>	<b>\$ 25.6</b>
Cash distributions declared – per Partnership unit (in dollars)	\$ 0.06	\$ 0.36

Note: <sup>1</sup> Comparative figures have been reclassified to conform to current year presentation.

**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 as reported in the GAAP financial statements, 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, and after provision for accrued capital expenditures.



Management 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, less actual 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.

Distributions are declared monthly with date of record on the last day of the month and payable within 15 days following.