

**Canfor Pulp Income Fund  
Q3 Earnings Conference Call  
October 25, 2006  
10:00a.m. ET**

**Operator:**

Good morning, ladies and gentlemen, welcome to the Canfor Pulp Income Fund conference call to discuss the third quarter earnings. Please stand by because this call is being recorded and webcast live on [www.Canforpulp.com](http://www.Canforpulp.com). A recording of the call and transcript will be available on Canfor's Pulp's website. Also, we would like to point out that this call will include forward-looking statements so please refer to the press release for the associated risks of such statements.

And with that I'd like to turn the call over to Mr. Paul Richards, President and CEO, of Canfor Pulp Limited Partnership. Please go ahead, Mr. Richards.

**Paul Richards - President and CEO:**

Thank you, operator. Good morning ladies and gentlemen. I would like to welcome you to our very first call. I would like to say also available to answer questions today are Tom Sitar, the CFO of the company and Rick Remesch, our Corporate Controller. Our comments today unless otherwise noted related to the operating entity Canfor Pulp Limited Partnership, which owns 20% of the Canfor Pulp Income Fund [editor's note:.Canfor Pulp Income Fund actually owns 20% of Canfor Limited Partnership]

First a comment on the third quarter overview. Third quarter for us was a great quarter for the Partnership. We had sales of over \$214 million, EBITDA of \$62.5 million, net income of \$41.9 million, and distributable cash of \$.70 per unit. The quarter also included \$5.9 million of one-time business acquisition costs, which Tom will discuss further.

Markets in the quarter were strong. Supply has been taken out and there has been strong demand from paper makers. NBSK Pulp prices reached 10-year highs during the quarter. NBSK Pulp inventory levels are now at 25 days, which is generally a strong level for the (inaudible) of the business.

We entered Q3 with all maintenance downtime taken earlier in the year. And on pulp operations generally all three mills ran well. We did have lost production for lightning strikes of about 7700 tonnes. But in spite of that it was our second best operating quarter ever. And because of that in general our costs were very good.

Paper operations also ran well in the quarter, making marginally more higher value paper -- bleach paper than the previous quarter.

And I'd like to also give a brief update on our Co-gen. We operated at 968 megawatt hours per date, which is 88% of capacity. As we noted before we continue to have two areas that keep us from running at 100% capacity. One in the Ash handling system of the power broiler and the other in the hog feed system. We have already purchased equipment that we think will resolve the ash handling system. We purchased it and we expect to install it in Q4 of this year. The cost was under \$700,000. We expect to have it up and running and optimizing in the first quarter and at full rate by second quarter latest. We hope to by the end of this quarter have purchased or identified and purchased the equipment we want to be installing for the hog feed system. We would expect -- I would hope to get it installed during our shutdown in Q2 next year and up and running by Q3. And I would like to be able to say that by Q4 we hope to be at 100% of full rate. We will see as we go along if we are able to meet that or if we fall slightly below or maybe even exceed the 100% target.

I'm going to hand the call over to Tom for a moment and I'll come back and make some comments around the markets as we see them going forward and fiber. Tom.

**Thomas Sitar - CFO and Secretary:**

Thank you, Paul. I will take -- just make some additional comments and provide just a bit of color on how we performed in the quarter.

You will note that this is our first reporting quarter, but since our year-end is December 31st, we are reporting it as our third quarter. And all of our comparatives provided represent NBSK business of Canfor Corporation prior to -- for all periods prior to July 1, 2006.

Paul mentioned EBITDA for the quarter was \$62.5 million, this was about \$35.7 million more than in the second quarter. So on a quarter-to-quarter comparison primarily better because of higher pulp and paper prices which was approximately an \$18 million improvement; increased productivity approximately \$11 million improvement; lower cost approximately \$10 million improvement and this partially offset by higher chip prices which was approximately \$3 million.

Going to our pulp segment, specifically in Canadian dollar terms, a list of price for NBSK delivered to northern Europe increased by approximately 6%. Our Canadian dollar net mill returns increased by approximately 10% in the quarter.

Higher sales returns leads to higher fiber costs and they were approximately 8% higher quarter-over-quarter.

As for productivity, second quarter was the lower as Paul mentioned, approximately 38,000 tonnes, because of the scheduled down time taken. No such curtailment was in the third quarter and we did lose the 7000 tons to lightning strikes.

In total pulp production was 257,000 tons in the quarter, which was approximately 13% higher. This higher productivity in the quarter lowered our conversion costs and we were approximately 19% lower in the third quarter compared to the second quarter in terms of cash conversion costs.

The segment pulp segment sales figure also includes agency fees that we earn on selling outbound pulp and Canfor (inaudible) pulp and that was approximately \$2 million as additional sales number booked in the quarter.

Turning to the pulp segment. Quarter-over-quarter improvement results 3% of -- higher sales prices and increased margin on our bleached paper, which is a high margin product. And again, productivity improvement also as a result of no downtime taken and that translated to approximately 3% on lower cash conversion costs.

The non-segmented or corporate items, those included a one-time and non-recurring \$5.9 million of what we describe in business acquisitions costs. These were costs incurred to establish the Partnership, the Trust and the Income Fund and to acquire the business from Canfor and they really consisted of legal, consulting and audit fees.

Couple other notes, the cash flow included interest cost of approximately \$1.8 million that was paid to Canfor on the note that we owed them \$125 million. Our expectation is to replace this in the fourth quarter probably the latter part of the fourth quarter with long-term debt of similar amount with commercial lenders and U.S. dollar private placement notes.

Capital spending. We expect for the year to be approximately \$22 million, of which approximately \$8 to \$10 will be spent in the fourth quarter. Any portion of the \$10 that will not be spent will be held back as a reserve for future spending. This is a much lower spending for the year than our stated objective of \$30 million per year. The reason for this is primarily due to lower strategic-type spending in the first half of 2006. We expect to get back to targeted levels in 2007 of approximately \$30 million. Of this, \$15 to \$20 million will be in maintenance type projects and the rest would be profit improvement projects. We do plan to maintain a reserve for future major capital projects at approximately \$4 million per year.

And lastly, we have no scheduled maintenance down time in the fourth quarter and for next year we expect that we will have down time in 2007 that will be approximately 7000 tonnes less than what we have taken in 2006.

Paul. That is what I have, back to you.

**Paul Richards - President and CEO:**

Thanks, Tom. Couple of comments now. First of all, on where we believe the market is today. Currently North America, Europe and Asia markets remain strong. Prices remain firm. We do see -- we are aware that there is hardwood coming online and we believe that pressure will begin in the Asian arena because of the potential to substitute for hardwood and that could begin by early as the beginning of this quarter.

Fiber supply. We do have concerns with the difficult lumber market and downtime being announced. This has caused market prices in our region to rise quarter-over-quarter from on the base price mid \$40 range in Q3 to today's level of below \$60, that is current market price in the region for the base price. It does not include transportation and other modest costs.

Fiber supply today for us is sufficient. We have chip inventory of about two weeks, which is certainly plenty under normal circumstances. In fact personally I would like to see fiber supply in the \$7 to \$10 dollar range [I mean]-- 7-10 day range when you have surplus supply and perhaps higher than two weeks if you are short. We are fairly balanced. However, my big concern is going to be for future announcement could be announced for downtime and in particular I'm concerned around the Christmas period, which my experience has shown that some mills tend to take more downtime if they have the opportunity. So we are initiated a program that says we would like to have the chipping facility made available up and running in November starting to deliver chips to offset what we consider would be some incremental down time in the Christmas period and that allows us to at least have the program developed and running. If more downtime should occur then we currently see or currently have been announced then we can ramp that program up and worst case scenario we are building up a little bit of a surplus if more down time is not enough.

The way that the housing markets are I don't know where it's going to go, but would like to be prepared in case if we see more announcements for down time. Cost for whole log chipping will be approximately \$20 above our highest cost fiber today. But that is an estimate. We don't know what the numbers will be and we will -- as we get into the program and see it could be -- I could be off by even 100%. I know it won't be 100% less, but we will have to see where that number comes out. But it will be higher. 50,000 tonnes value is above 2% of total supply, but we're really concerned around the Christmas period in case there is downtime in that area.

Finally I'd like to make some comments on cash distributions. As announced yesterday in our press release, due to strong markets and operations the Canfor Pulp Income Fund for October will be distributing 12 cents per unit plus a supplemental distribution of 8 cents per unit. This brings total distributions in the first four months of the Fund to 64 cents per unit. Strong markets and good operations should allow Canfor Pulp to continue with its current program of monthly and supplemental distributions for the balance of 2006.

So in summary, overall Q3 was a very good quarter. Prices were high. The mills ran well. Costs were in control.

So I'd like to thank you for participating on the call and operator, we are now ready to answer questions.

**Operator:**

We'll now take questions from the telephone lines. We'll first take questions from the financial analysts followed by the media. If you have a question please press \* 1 on your telephone keypad. If you are using a speaker phone lift the handset and then press \* 1. If at any time you wish to cancel your question please press the pound sign. Please press \* 1 if you have a question. There will be a breeze pause while participants register for questions. Thanks for your patience.

The first question is from Mark Bishop of RBC Capital Markets. Please go ahead.

<Q>: Thanks. Good morning, Paul and congratulations for a good first quarter.

A couple of questions, actually several but I will take a few and get back in the queue. The first one is just around your geographic market mix. The sales realization was certainly higher than we had forecast. I'm just wondering if part of that may have been a skewing or more volume into the U.S. and Western Europe than maybe we had seen in the past?

<A>: Mr. Richards: Depending on which past you are looking at, I don't think a lot of change from Q2 to Q3, but from last year to this year we have been generally growing in North America. We have gone from probably around 40% or so in North America to much closer to 50% today and with an off-set reduction generally in the Europe so we have been picking up in the region that has higher price and also the area that has seen more downtime taken.

<Q>: So the 50% in North America, is that more or less what we're going to see for the foreseeable future?

<A>: Mr. Richards: Whys, I think 2007 will mirror that number.

<Q>: Okay. Question for either Paul or Tom. The cash distribution obviously represented only 63% of your distributable cash. Is there a plan for the cash that was built up between the 63 and sort of the target 90% payout? Do you have plans for that additional cash beyond the reserve for the boiler?

<A>: Mr. Sitar: Well, you have to remember that the way we have discussed how we're going to make distributions. It is both the reserve for the \$4 million in capital expenditures, you can call it boiler, but we're really treating it as major capital in the future. So \$4 million for that and reserve of approximately their 10% at sort of cash hold-back. We said we would distribute around 90% of what is the remaining after the provision for the \$4 million. So we plan to get to that rate by the end of the year. And in this particular year the difference may be a little bit since the capital spending wasn't quite at the rate that we would expect on a full-year basis that reserve for capital may be slightly higher just to account for the fact that we didn't get all the capital spending done that we had anticipated.

<Q>: Okay. So the 90% is still a target pay-out ratio?

<A>: Mr. Sitar: Yes, it is.

<Q>: Okay.

<A>: Mr. Sitar: After provision for those items.

<Q>: Right. On the unallocated cost that we saw in the quarter of \$3.9 million is that a level that we should be looking at annualizing going forward?

<A>: Mr. Sitar: Probably the better one I would lead you to is our SG&A number in the income statement as a number and that is a good number. We have 5.5 in there for the quarter, that is a good number to use as an ongoing rate.

<Q>: Okay. Just finally one last question for you, Paul. I see this morning IP has announced a joint venture with Ilam in Russia. Just wondering if you have comments or thoughts on that that might change the landscape of particularly the Russian participation in the market, the way they may behave going forward?

<A>: Mr. Richards: No, I have no comments on that.

<Q>: Okay. Thanks very much.

**Operator:**

Okay. The following question is from Patrick Yung of Raymond James. Please go ahead.

<Q>: Good morning. Congrats on the strong quarter. Just a question on the fiber costs. Could you go into a bit of detail about your fiber supply agreement with Canfor? My understanding is Fiber cost — or fiber prices are set until I think August of next year. So would the fiber cost inflation right now not impact Canfor Pulp?

<A>: Mr. Richards: Well, the agreement we had with Canfor had a formula that says this is where we expect that market prices will be. But that we have always said that we would have a market price. And occasionally things happen that the market has changed a little bit from what we anticipated, but we still need to be at market. So what we've done is we've taken a look at what we believe to be the market price and we've adjusted from the base formula up to say the base formula doesn't truly represent market. We do believe and we're not only talking about our major owner in here, but all our suppliers. We cannot be in a position -- and we by the way, we have the same agreement everyone of our suppliers, so it is not just Canfor. We cannot put them in a position that they are disadvantaged to their competitors which could result in them taking more downtime. We can't afford to be in that position so we see must paying at a market price to make our suppliers as competitive as others in the region. So we have a formula that keeps us -- and for the last year has worked very well, but in this unusual situation with a lot of people taking downtime it doesn't truly reflect the mark yet we've had to make an adjustment to make sure we stay within the market.

<Q>: All right. Thanks for that. And should we be factoring in any cost associated with setting out the log chipping facility in Prince George?

<A>: Mr. Richards: Well, there will be cost. I don't know how much of it will show up in Q4 quite frankly. We will not do all of the chipping in Q4. We will do some in next year. And even the chipping that we do in Q4 it needs to go on a pile and it won't all show up. So some portion of the cost will be here. I don't know if it is 10% or 50%, it certainly won't be more than 50 and some will carry forward into the next year. So there will be a modest cost in the future.

<Q>: All right, that is helpful. Final question is on strategy. Any thoughts on growth strategy, acquisition or paying more attention to strategic upgrades or things of that nature?

<A>: Mr. Richards: Yeah, right now we have a group of people at the Knolls(ph). We have a very good group of people actively looking at where we can optimize our operations and I'm not just talking about the modest creep we've seen in the last few quarters. We will continue to do that in modest improvements. But we're looking at is some hit that is might be 2, 3, 5 million dollar costs that gets us some bigger returns. And we really do want to

generate some ideas and move forward with those. So we expect to have some of those reflect out by Q1 of next year and hopefully be able to implement in the next year, but I don't see major changes for '07, but I would hope that we're able to come up with idea that is move us forward in '08. Those events in the strategic area we are looking at now. We are not looking outside that arena.

<Q>: All right. That's all I had. Thanks a lot.

<A>: Mr. Richards: Okay.

**Operator:**

Once again financial analysts may press \* 1 for questions or comments. The following question is from Paul Quinn of Salman Partners. Please go ahead.

<Q>: Thanks very much and congratulations on a good start. Just a question on down time schedule for 2007. Which mills are going down which quarter

<A>: Mr. Richards: Well, we do have a list but frankly following this call I begin two days of review at the mills and we'll be going over some of those things so they are not finalized. But I think in principal we are looking at less down time than we had last time. I think Paul mentioned mentioned 7000 tons less. Certainly there will be less at Northwood because we have our major last year. But we will be taking mini-shutdowns this year and probably a little bit more at Intercon and the same in Prince George.

<Q>: Okay. Could you -- just on the chip cost here you mentioned you expect a whole lot chipping to be -- what did I write down \$40 bucks, \$20 bucks a ton more than your highest cost. Where do you get that estimate?

<A>: Mr. Richards: Well, what we do is we estimate what the delivering the pulp log to the chipping facility would be. We estimate the cost of chip and deliver to the mill. We put that all together and we compare it with what we know our cost are being delivered to the mills today from our various suppliers. Where we're unsure -- in the past we have done in chilling here and other locations have been the numbers might have been a bit lower. I think the cost would be higher initially and I'm hoping that it will drop off as we get a little bit more accustomed to and get it back at and if we have to increase the volume I also hope the cost of the facility will also drop off.

<Q>: Okay and in terms of the chipper that you're going to set up, it is a 50,000 tonnes per year machine?

<A>: Mr. Richards: No, no, no. It's a -- I don't know the total capacity. My guess is total capacity itself is in the hundreds of thousands. It is located at one of our saw mills. 200,000 I'm told. And we have another one available at another saw mill both are of these are Canfor operations. And so we're only setting up now for what we want to cover through the Christmas period.

<Q>: Oh, okay, I understand that. Just a comment on just overall paper markets, what you are seeing on that side?

<A>: Mr. Richards: You know, we had announced the price increase in paper and we're trying to move that through. So we see it being pretty steady. Don't see any major changes one way or another. I would say that I would be looking at it being similar next year to this year.

<Q>: Okay. Great. Thanks, guys.

**Operator:**

Thank you. The following question is from Herve Carreau of CIBC World Markets please go ahead.

<Q>: Yes, thank you. Just another clarification on the chip prices. Did your number for quarter full year reflect the increase that you mention from \$44 to \$60 per ton or sore is that something you will see in Q4?

<A>: Mr. Richards: Um, I am not sure of the question, but I will answer this way. The number reflected where prices are in October for sure. I don't know where they will be in November and December.

<Q>: Okay and with the additional cost resulting from the chipping, is it fair to say under worse case you won't see your chip prices increasing by more than \$20 a ton or from today's level? Is that a worst case or --

<A>: Mr. Richards: I don't know about that, I think there are so many factors that come into play in terms of the volume we might need to use. I don't know that I would want to comment on where they could potentially go.

<Q>: Thank you.

**Operator:**

Thank you. There are no further questions from the investment community. We'll now take questions from the members of the media. If you have a question please press \* 1 at this time.

There are no questions registered from the media. I would now like to turn the meeting back over to Mr. Richards.

**Paul Richards - President and CEO:**

Well, thank you very much, operator, and I would like to thank everybody for participating on the call and again I hope that from our perspective we can continue to perform as well as we have and that our business stays as strong as it has been for the last quarter. Thank you very much for being on the call.

**Operator:**

Thank you gentlemen, the conference has now ended please disconnect your lines at this time. We thank you for your participation and have a nice day.