

**Canfor Pulp Income Fund  
Q3-2009 Conference Call  
8:00am (Pacific) October 26, 2009**

**Company Participants:**

- Paul Richards, President & CEO
- Terry Hodgins, CFO & Secretary
- Joe Nemeth, Vice President, Sales & Marketing
- Brett Robinson, Vice President, Operations

**Operator:**

Welcome to the Canfor Pulp Income Fund 3<sup>rd</sup> Quarter 2009 Results Conference Call. Management's comments today unless otherwise noted relate to the operating entity Canfor Pulp Limited Partnership which Canfor Pulp Income Fund owns 49.8%.

Please be advised that the call is being recorded and webcast live on the company's website, canforpulp.com. A recording of the call and the transcript will be available on the company's website as well. The company would also like to point out that this call will include forward-looking statements, so please refer to the Friday, October 23, 2009 press release for associated risks of such statements.

I would now 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:**

Well thank you, Operator and good morning ladies and gentlemen. Thank you for joining us today. On the call with me are Terry Hodgins, our CFO, Joe Nemeth, our vice-president of sales and marketing and Brett Robinson our vice-president of operations. I'll offer some comments on the third quarter after which Terry will provide his financial commentary and I'll return with some further updates on Q4.

On Friday we reported for the second quarter, sales of \$202 million, net income of \$18.3 million, EBIDTA of over \$20 million and adjusted distributable cash of 16 cents per unit. The gradual improvement in consumption and continued curtailment of the supply of pulp has led to steady

reductions in world pulp supplier inventories which were reported at 22 days for softwood pulp for September. The tightening market has enabled suppliers to increase prices in each of the last five months. North America list prices have increased from USD \$660 in June to \$770 in September with announcements of \$800 for October and \$830 for November. Unfortunately the weakening US Dollar had diminished some of the benefit of improved prices for Canadian and European producers. During the quarter the US Dollar declined in value by 6% in relation to the Canadian Dollar. Nevertheless average North American list prices converted to Canadian Dollars increased \$50 per ton compared to the second quarter.

Now to our operations. During the third quarter we had no scheduled maintenance shuts and mills ran generally well. Market pulp production for the quarter at 264 thousand tons exceeded both the previous quarter and third quarter of 2008. Manufacturing costs in the third quarter are typically at the lowest levels of the year due to the favorable operating environment and lower energy consumption. This combined with lower chemical prices and the benefits of our cost reduction program enabled us to generate much improved results. Fiber costs in Q3 were flat as compared to the second quarter. Residual chip prices have risen with rising pulp prices while whole log chip costs have come down. Chip inventory volumes are quite high with more than 5 weeks supply. With US housing starts still at low levels keeping lumber prices depressed and a high Canadian Dollar, we will maintain the additional inventory until the new year in anticipation of sawmill curtailments over the Christmas period being extended.

I'll now hand the call over to Terry and following his financial summary will return with some additional comments. Terry?

**Terry Hodgins:**

Thank you, Paul. Details and commentary of the third quarter results are in Friday's press release so I won't take you through all the details but would like to highlight some specific items that are in fact on the financial results. For the third quarter, the partnership quoted EBITDA of 25.1 million compared to 7.2 million in the previous quarter. You'll recall included in the second quarter EBITDA was 3.5 million on settlement of the insurance claim relating to the Prince George pulp and paper fire in 2008. Other elements comprising the change in quarter-over-quarter EBITDA are approximately 10.4 million from increased pulp prices. And this is net of currency exchange impact. Approximately 2 to 2 and a half million dollars each from lower chemical costs, lower spending on fixed costs and higher quarter-over-quarter production

volume. The remainder of the difference in the results quarter-over-quarter are from absorbing higher cost opening finished pulp inventories in the second quarter. While the pulp segment showed an 18.3 million quarter-over-quarter increase in EBITDA, the paper segment's EBITDA was essentially flat. Increased sales and production volumes and reduced manufacturing costs were offset by a 6% decline in realized paper product selling prices when translated to Canadian Dollars. During the quarter we completed a new 40 million bank credit facility with a maturity date of November 30, 2011. In addition we arranged a \$25 million letter of credit facility subject to completion of legal documentation. To ensure we maintained financial flexibility during the renewal process we intentionally conserved our cash as a precaution in the event of any delays or issues arising in the renewal period. This cash buildup was accomplished through the timing of payments of chips and corporate services. As a result we ended the quarter with 43.9 million in cash and no cash draws on the operating line. At September 30 utilization of the new credit facility consisted only of 16.5 million in letters of credit issued to BC Hydro. Since the quarter end, our cash balances have returned to more normal levels and we expect only limited if any cash draws on the credit facility through the remainder of the year. The financial covenants under the new financing arrangements are similar to those under our long term note agreement which consists of a leverage and an interest coverage test. We remained in compliance with the covenants as of September 30 and based on projections we expect to remain in compliance for the foreseeable future. The operating credit financing renewal had no impact on our long-term note agreement which is unchanged and remains in place with maturity date of November 30, 2013. We continue our focus on cash and working capital management. Pulp inventories increased marginally during the quarter but remain within our target range. Investment in wood chip inventories increased \$7 million from the low point in June but are at similar dollars to this time last year. As Paul explained, chip inventory volumes have been intentionally increased to protect against possible sawmill curtailments. Capital expenditures for the year are expected to be in the \$16 million range. The cash distribution for the month of November payable in mid-December will be announced on or before November 19 in accordance with our regular reporting schedule. Regarding the change in taxation of flow-through trusts, we continue our process of review and our evaluation of alternatives to the current structure. At this time our view has not changed and absent any developments we would expect to convert to a corporation on January 1, 2011, the date that the tax changes come into effect. Back to you, Paul.

**Paul Richards:**

Thanks, Terry. As we have previously reported, we had scheduled downtime maintenance at the Northwood Mill in the fourth quarter. Planned outage was scheduled for additional work on the recovery boiler which would result in a total reduced production of approximately 31 thousand tons. This work has been completed and the mill is now up and running at full rate. There are no other maintenance shuts planned for our mills in the fourth quarter. As stated earlier, pulp prices have risen steadily with a most recently announced list price in North America for November being \$830 US. China demand was very strong in the first half of 2009 and other regions have showed growth trends in Q3. Supply constraints remain a key factor in current markets as rising producer currencies have limited the startups of high-cost producers who curtailed their production in Q1 and Q2 of this year. We expect markets to remain firm at least through to the spring of 2010. On October 9 the Federal Government announced the allocation of credits under the billion dollar pulp and paper green transformation program. Partnership has been allocated \$122.2 million to be spent on qualifying energy and environmental capital projects by March 31, 2012. In anticipation of this announcement we have identified and will be promptly submitting a number of projects for program approval that include improvements in air emissions, both odor and particulate, and improvements in energy efficiency. Included in the projects is the Northwood recovery boiler upgrade which would consume more than half of the available credits. This project will require environmental assessment approval which may delay commencement. We expect that funding will begin to flow from the program on a cost reimbursement basis sometime before the first half of 2010. In addition to environmental improvements, we expect economic benefits from these programs reflected in operating and financial results beginning in 2011. In closing, we remain committed to our cost reduction and working capital management programs. We expect market conditions to show continued but modest improvements for the remainder of the year and beginning of 2010. Operator, that concludes our prepared comments and we are now ready to take questions.

**Operator:**

Thank you. We will 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 push \*1 on your telephone keypad. If you are on a speakerphone, please lift the handset and then hit \*1. If you wish to cancel your question please push the pound sign. Please press \*1 at this time if you

have a question. There will be a brief pause while participants register for questions. Thank you for your patience.

The first question is from Paul Quinn of RBC Capital Markets. Please go ahead.

**Paul Quinn:**

Thanks. Good morning, guys. Question about the BC Hydro energy agreement that you signed... understand you made a payment. I'm just trying to understand the economics of your energy purchase agreement if you could help me out with that.

**Paul Richards:**

Well, high level, what we did was on the original agreement we had with Hydro we each submitted a certain dollar value and we wound up with the ability to produce power at a certain rate. That did not meet our original projections and what we did as – what Canfor Pulp did was spend additional funds to get to the original level of power generation. With Hydro we had the option to pay a penalty for not meeting the original levels which is what we opted to do recently so that we could then sell that at a higher rate.

**Paul Quinn:**

Ok so that extra 52 gig watt hours you were able to sell at what rate under the energy purchase agreement?

**Paul Richards:**

That's just slightly over \$100 a megawatt hour.

**Paul Quinn:**

... per megawatt hour... Ok, in terms of the green transformation program I understand an environmental assessment is required for big projects, is that going to slow you down at all?

**Paul Richards:**

Well first of all, it's required for all projects because it's federal funds.

**Paul Quinn:**

Right. And there will be some slowdown – I'm not sure if that's the right term. I think that fundamentally some of these projects are relatively small so they should go fairly quickly. We would expect the majority of these projects to be gone and almost completed in 2010. But the big one, the Northwood recovery boiler, because it's so large and is – will have actually all positive impacts on the environment still requires some assessment. And that will take some time. We believe that it shouldn't keep us from completing the project by the timeframe of 2012 but we are aware that we must move quickly to be able to begin construction and complete it by the end of 2011. We need to get that project done before the actual date in 2012 because of the winter season.

**Paul Quinn:**

OK, so in terms of that environmental assessment have I got it right, that's like a 4 to 6 month process?

**Paul Richards:**

I don't think it has to be quite that long. That would be on the long end of it.

**Paul Quinn:**

OK. And just lastly, in terms of the conversion to a C Corp January 2011, how should we model that? Is there any losses we can carry forward to 2011 or is it fully taxable at that point?

**Terry Hodgins:**

Paul, we wouldn't anticipate having any losses that we could carry forward at that time. I think you should consider it to be fully taxable for your models.

**Paul Quinn:** Thanks very much. Great quarter!

**Paul Richards:**

Thanks.

**Operator:**

Thank you. Once again please press \*1 if you have any questions or comments. The next question is from Stephen Atkinson of BMO Capital Markets. Please go ahead.

**Stephen Atkinson:**

Thank you. Can you give us a small color on the Northwood recovery boiler, like is this a brand new one?

**Paul Richards:**

No, no. This was just regularly scheduled work. Now we originally intended for it to be longer than normal. We wanted to do some incremental work. We've been regularly doing some work in the boiler to try to basically extend the life in the main burning section. So we went in to take a look at the boiler. We knew we were going to take additional downtime compared to normal and as we got in we discovered areas that we decided we would repair now and basically get the boiler back up to really good shape going forward so. And this is not areas that we in terms we'd be going after so we've been doing a lot of overlaying of the boiler, rebuilding in around the floor area in the walls and this was again scheduled work, just more than we had anticipated.

**Stephen Atkinson:**

So then when we're talking about the green transformation program, that is a major project is it?

**Paul Richards:**

Yes and in doing a green transformation project, what we are effectively doing is what we call a low odoring the boiler. And low odoring the boiler means that there are some new sections of the boiler that would be put in, economizer sections, there will be a lot of extra tubes, we will be taking out the direct contact cascade evaporator and putting something else in a lot of areas... however there are some areas of the boilers that do not need to be changed and in those areas we are trying to make upgrades so that we have a boiler that is in very good shape.

**Stephen Atkinson:**

And would you, would there be any return on it, you know, can you generate any more power or anything from all of this?

**Paul Richards:**

There will definitely be economic returns on the recovery boiler around the energy side. It's much more energy efficient so just the way we produce steam and power will be lower cost. There will be, we expect a significant return – minimally at least 10% on that boiler.

**Stephen Atkinson:**

Ok and so that where you have paid some money I guess to BC Hydro in the near term to reduce, as it were, the commitment, then you will be able to increase the commitment? Is that how it's going to work or how would you do it? You'd be able to sell more power at \$100 per giga watt hour?

**Paul Richards:**

No, not on this boiler. We have no agreement with Hydro. We are talking to them about the potential to produce more power and at higher levels but we have not made any agreements on the Northwood site. All of the – the agreement we have today is on the PG Intercon site.

**Stephen Atkinson:**

OK. And so that could be some upside down the road.

**Paul Richards:**

That's correct.

**Stephen Atkinson:**

In terms of where you took 1000 tons of production downtime as it were this quarter, will you be reducing the working capital to should we say offset that?

**Paul Richards:**

I wouldn't expect so. No.

**Stephen Atkinson:**

OK. Thanks very much.

**Operator:**

Thank you. There are no further questions registered at this time. I would now like to turn the meeting back – I'm sorry. The next question is from Gordon Hopestar from Prince George Citizen. Please go ahead.

**Gordon Hopestar:**

Hello. Good morning, gentlemen. Quick question on the 122 million. You mentioned that it triggers a federal environmental review because of the funding obviously. Is that the same for the BC process and do you have any sense for how those two will work together?

**Paul Richards:**

That's a good question. We're hoping that the BC and the feds can get together and we'll go through one process. I think there's still discussions around that but either way there will be a process review for every project.

**Gordon Hopestar:**

And do you have a sense – you've talked about the Northwood project, you know like a list of the exact projects of the other ones you're going to do and if not, sort of when you'll be laying out a list of those projects?

**Paul Richards:**

Yeah, we have a couple of projects that are virtually we will go through with no matter what. They're not in the same order of magnitude as Northwood with those kinds of dollars but we're definitely looking at low odor projects which is a little bit lower in total cost, probably close to the \$10 million range but strictly in odor reduction that will be, will have a big impact on the community. That one will probably go through regardless of any issues that we see. We have some other energy projects that we're looking at that will probably go through regardless of the impact. They're relatively small. We don't see those as issues. We're also looking at specific particulate reduction ones but on the ones that are in the lower range in the let's say \$5 to \$10 million we'll go through with those relatively quickly. The Northwood one we just have to see how that one unfolds through the process.

**Gordon Hopestar:**

With that other project are they on the PG Intercon site?

**Paul Richards:**

One of them for sure is. Yes, one of them for sure is.

**Gordon Hopestar:**

OK. And the Northwood project, does that include putting an ESP on the boiler as well?

**Paul Richards:**

Well it definitely looks like we're going to make changes on the ESP whether we put a new one on or rebuild that's one area we're looking at for sure.

**Gordon Hopestar:**

OK.

**Operator:**

Thank you. The next question is from Benoit LaPlaid from Scotia Capital. Please go ahead.

**Benoit LaPlaid:**

Thank you. Good morning. Terry, your chemical costs were down significantly on the quarter. Just curious to understand why given it's a cost plus contract that you have and what would be the outlook for coming quarters? Similar levels or is it a seasonal issue with power costs? Or?

**Paul Richards:**

I'll answer that one, Benoit. Couple of things. Not all of our chemicals are cost plus. Some are some are not. So some of our chemicals, we've seen lower prices. It's really a lag from lower energy prices so that's pretty significant. In addition, late last year we went, we did some considerable work around trying to reduce chemical usage which is also a big factor. So we're seeing both reductions in cost and usage.

**Benoit LaPlaid:**

So that should stay relatively flat for the coming quarter.

**Paul Richards:**

Yes it should.

**Benoit LaPlaid:**

Great. Thank you.

**Operator:**

Thank you. There are no further questions registered at this time. I would now like to share our meeting back to Mr. Richards.

**Paul Richards:**

Well thank you very much, Operator. I would like to thank everybody for being on the call today with us. And again, if you have any questions please don't hesitate to give us a call. Thank you very much.

**Operator:**

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