

## **CANFOR PULP INCOME FUND ANNOUNCES FOURTH QUARTER AND 2006 RESULTS, FEBRUARY DISTRIBUTIONS**

February 16, 2007 – Vancouver, B.C. – Canfor Pulp Income Fund (the “Fund”) (TSX:CFX.UN) announced today its fourth quarter and six month results as well as the results of Canfor Pulp Limited Partnership (the “Partnership”) in which the Fund has a 49.8% ownership.

The Partnership had net sales of \$229.0 million, net income of \$44.8 million, or \$0.63 per unit, and EBITDA of \$61.9 million, or \$0.87 per unit, for the quarter ended December 31, 2006. These results, which are similar to the prior quarter, reflect improvements in NBSK pulp pricing in all markets, the benefits of a weaker Canadian dollar and improved results from the kraft paper business, all of which were offset by higher costs. The increased costs in the fourth quarter, when compared to the prior quarter, were primarily due to fibre costs, and, in addition, to a seasonally normal increase in the use of energy, increased costs for maintenance due to the timing of several routine projects and to higher administration costs. When compared to the fourth quarter of 2005, costs were lower with the exception of fibre.

The Partnership's mills ran well with no significant maintenance downtime in the quarter. Total pulp and paper production was 8,100 tonnes above the prior quarter and 10,600 tonnes better than the same period last year. On an annual basis the mills produced at a record level, more than 20,000 tonnes above the previous record set in 2004. Paul Richards, President and CEO of the Partnership, commented: “we are pleased with the record level of performance of our mills and the reduction of controllable costs.”

The cogeneration system at the Prince George Pulp mill executed a planned maintenance outage in December and electrical power production was curtailed for the installation of modifications to the ash handling system.

Fibre costs increased during the quarter, driven by a rise in pulp mill sales returns, and, in addition, by market conditions brought about by a reduction of sawmill residual chip volumes due to the slowing lumber markets. A small component of the cost increase was also due to the production of roundwood chips. This program was initiated in the fourth quarter of 2006 to replace sawmill residual chip reductions and will continue for the next few months. The Partnership may continue the roundwood chipping program in the second half of the year depending on the sawmill operating environment.

“The market outlook for the first quarter of 2007 is positive, as price increases have been announced for NBSK pulp in all markets and inventories remain low. A continued risk remains the level of supply of residual chips as lumber prices remain under pressure. Given our continued low cost and efficient operations, we believe that we are in a relatively strong position to cope with this risk”, said Mr. Richards. Also in the first quarter of 2007, the Partnership plans to reduce pulp production by about 8,000 tonnes for scheduled maintenance in late March. However, total lost production due to scheduled maintenance for the full year 2007 is expected to be 5,000 to 10,000 tonnes less than during all of 2006. Shutdowns will be spread through the year rather than concentrated in one quarter, as was the case in 2006.

On February 10<sup>th</sup> the union representing Canadian National Railway's (CN) train conductors and yard service crews commenced strike action. CN is continuing service with management personnel. While there have been no service interruptions to date, the Partnership is dependent on CN's rail service for its shipment of finished products (pulp and paper) and inbound deliveries of chemicals and fibre. Contingency plans are in place for both inbound and outbound transportation, but we are concerned about potential problems if the dispute continues for any length of time.

To update on the previously disclosed equipment malfunction in the bleach plant at the Intercontinental Pulp mill, replacement equipment has been delivered on site with repairs progressing well. Bleached pulp production is expected to resume within a week.

The Fund also announced that it will continue with its monthly distribution of \$0.14 per Fund unit, which for the month of February will be paid on March 15, 2007, to unitholders of record at the close of business on February 28, 2007.

The Fund declares distributions on a monthly basis with the record date on the last day of each month and payable within the 15 days following. These monthly distributions are intended to be equal to the monthly distributions of the Partnership on which they are dependent. The Partnership's cash distributions are based on estimates of cash flow from operations, less capital spending and a reserve for future major capital expenditures. The Partnership periodically reviews the level of its cash distributions, taking into account current and expected future performance and cash flow requirements. In 2006, for the first six months of its operation, the Partnership declared total distributions of \$1.24 per unit representing approximately 80 per cent of its distributable cash. The Fund declared corresponding distributions of \$1.24 per fund unit or \$30.4 million for the period from July 1 to December 31, 2006.

## SUMMARY OF SELECTED PARTNERSHIP RESULTS

(millions of dollars, except for per unit amounts, unaudited)	Q4 2006	Q3 2006	Year 2006	Q4 2005	Year 2005
Sales	229.0	214.3	834.4	195.9	771.2
EBITDA	61.9	62.5	184.1	29.0	63.9
Operating income	49.3	49.7	135.1	16.7	16.7
Net income	44.8	41.9	123.0	16.6	16.5
Per Partnership unit, basic and diluted					
Net income	0.63	0.59	1.73	0.23	0.23
EBITDA	0.87	0.88	2.58	0.41	0.90
Average Canadian/US exchange rate <sup>1</sup>	0.878	0.892	0.882	0.852	0.825

EBITDA decreased by \$0.6 million over the previous quarter, and was \$32.9 million better than in the same quarter in 2005. NBSK pulp prices remained strong, with net realized prices in Canadian dollar terms increasing by 4% during the fourth quarter and by 18% when compared to same quarter a year ago. Offsetting the favourable market conditions were higher costs for fibre, the seasonal increase in energy costs, higher corporate administration costs and higher maintenance costs.

## OPERATING RESULTS BY BUSINESS SEGMENT

### Pulp

(millions of dollars unless otherwise noted, unaudited)	Q4 2006	Q3 2006	Year 2006	Q4 2005	Year 2005
Sales	197.6	187.4	720.9	168.2	653.8
EBITDA	62.1	64.5	191.3	29.8	70.1
EBITDA margin	31%	34%	27%	18%	11%
Operating income	50.6	52.7	146.3	18.5	26.7
Average pulp list price – US \$ <sup>2</sup>	730	711	683	600	611
Average pulp list price in Cdn \$	831	797	774	704	741
Production – pulp (000 mt)	263.7	257.5	1,015.4	255.4	983.2
Shipments – Partnership-produced pulp (000 mt)	249.8	251.4	1,001.5	260.7	982.1
Marketed on behalf of HSLP & Canfor (000 mt)	128.3	149.4	570.6	149.1	579.9

Operating income of the pulp segment decreased by \$2.1 million from the previous quarter and improved by \$32.1 million when compared to the same quarter in the prior year. Improved performance at all mills over the prior quarter, improved NBSK price and a slightly weaker Canadian dollar were the main drivers of the improved results. These were offset by higher fiber costs driven primarily by weak lumber markets, which precipitated sawmill downtime and subsequently a temporary shortage of residual chips, higher energy costs, and higher maintenance costs due to the timing of several routine projects. When compared to the prior year the benefit of an 18% increase in Canadian net realized price was reduced by lower sales volumes and higher fibre costs.

### Operations

An annual production record for total tonnes highlighted 2006, surpassing the previous record by 20,000 tonnes. NBSK production during the fourth quarter was higher by 6,200 tonnes over the prior quarter and 8,300 tonnes over the same quarter in 2005. The increase was due to improved performance and reliability at all facilities. There was no

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

<sup>2</sup> Per tonne, delivered to Northern Europe

maintenance downtime in either quarter. The increase over the same period in 2005 was primarily the result of maintenance downtime in 2005 including the reduced production at the Prince George pulp mill during the cogeneration project ramp up.

The cogeneration facility at the Prince George Pulp mill averaged 877-megawatt hours per day during the fourth quarter compared to 968 in the prior quarter and 898 in the same period last year. In December, a four day outage for the installation of improvements to upgrade the ash handling system contributed to the reduced power generation during the fourth quarter. We expect to make additional modifications to the cogeneration system during 2007 to further improve its performance.

### *Markets*

The Partnership experienced strong demand for pulp during the fourth quarter of 2006, following very strong demand in the preceding quarter. This was partly driven by above normal consumption from Europe and Asia but mostly due to the large reduction in Canadian NBSK production capacity (approximately 1 million tonnes or 16% of Canadian capacity was shut in 2006). The capacity reduction was primarily the result of mill closures in Eastern Canada due to high fibre and energy costs and the strengthening Canadian dollar.

The benchmark price for NBSK pulp delivered into Northern Europe stood at US\$710 per tonne at the end of September 2006, and rose to average US\$730 during the quarter. Inventory levels for NBSK pulp fell 1 day to 24 days of supply, with 30 days of supply generally considered to be a balanced market.

### *Outlook – Pulp Markets*

In January 2007, list price increases were announced in all markets. For Northern Europe a US\$30 to US\$40 increase was announced, which will take prices to US\$760 to US\$770 per tonne. In the United States, a US\$20 increase will bring prices to US\$790. The Asian markets also saw a US\$20 list price increase announcement, which would take prices to US\$730 to US\$760 depending on the country of delivery.

Looking ahead into 2007, we believe that demand and pricing will hold up well through the first half of the year. While global economies are projected to slow somewhat, the year is beginning with very low global inventories and the NBSK market is expected to continue to be in short supply. Some moderation in prices in the second half of 2007 may occur.

### **Paper**

<i>(millions of dollars unless otherwise noted, unaudited)</i>	<b>Q4 2006</b>	Q3 2006	<b>Year 2006</b>	Q4 2005	Year 2005
Sales	<b>31.4</b>	26.9	<b>113.5</b>	27.7	117.4
EBITDA	<b>3.6</b>	0.9	<b>7.0</b>	2.7	7.4
EBITDA margin	<b>11%</b>	3%	<b>6%</b>	10%	6%
Operating income (loss)	<b>2.6</b>	(0.1)	<b>3.2</b>	1.7	3.6
Production – paper (000 mt)	<b>33.9</b>	32.0	<b>129.1</b>	31.6	127.4
Shipments – paper (000 mt)	<b>32.8</b>	29.5	<b>124.6</b>	30.6	127.2

Operating income of the paper segment improved by \$2.7 million from the previous quarter and \$0.9 million when compared to the same quarter last year. Net realized price in US dollars increased by 3% over the prior quarter and 11% over the same period a year ago. Price increases and higher sales volumes were partially offset by higher costs for slush pulp, which is transferred at market price.

### *Operations*

Paper production during the fourth quarter was higher by 1,900 tonnes over the prior quarter and 2,300 tonnes more than the same quarter in 2005. The increase in productivity was due to improved paper machine efficiency. Paper production for the year was 1,700 tonnes above 2005.

### Markets

Kraft paper pricing and demand remained steady in the quarter with sales matching production. We continue to grow our shipments into the North American market, specifically in the higher margin bleached products. Tight supply was the main driver of the strong kraft paper market throughout 2006.

### Outlook – Kraft Paper Markets

Kraft paper markets are expected to remain strong throughout 2007, as the demand supply balance is still tight on the supply side. A further price increase for bleached kraft paper is expected in the second quarter of 2007.

### Non-Segmented Items

(millions of dollars, unaudited)	Q4 2006	Q3 2006	Year 2006	Q4 2005	Year 2005
Unallocated costs	3.9	2.9	14.4	3.5	13.6
Business acquisition costs	-	5.9	5.9	-	-
Net interest expense	2.0	1.8	3.8	-	-
Foreign exchange loss on long-term debt	2.5	-	2.5	-	-
	8.4	10.6	26.6	3.5	13.6

### Unallocated Costs

Unallocated costs, comprised principally of general and administrative expenses, totalled \$3.9 million in the fourth quarter compared to \$2.9 million in the prior quarter and \$3.5 million in the same period last year. Unallocated costs were higher than those in prior periods as a result of higher administrative costs including audit fees, salaried employees incentive plan and legal fees. The administrative costs in prior year comparative periods primarily represent allocations of Canfor's corporate administration, legal services, human resources, treasury services and incentive plan amounts. These were based on estimates of the pulp business' share of Canfor's corporate costs. A refund of provincial sales tax of \$1.1 million reduced unallocated costs in 2005.

The Partnership incurred costs related to its initial organization and the acquisition of the Pulp Business from Canfor, fully described in Note 1 to the Partnership's financial statements, principally comprised of legal, accounting, audit and consulting fees.

### Interest Expense

Net interest expense of \$2.0 million during the fourth quarter reflects two months at prime rate plus 0.5% paid to Canfor for borrowing under the \$125 million promissory note and one month at 6.41% due to the holders of the US\$110 million (Cdn\$125.7 million) notes issued on November 30, 2006. The interest expense is net of interest earned on cash and cash equivalent investments. No interest expense is shown for periods prior to July 2006, since the Pulp Business was an integral part of Canfor and interest was not allocated to it.

## SUMMARY OF FINANCIAL POSITION

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

( millions of dollars, except for ratios, unaudited)	Q4 2006	Year 2006	Q4 2005	Year 2005
Ratio of current assets to current liabilities	1.92	1.92	2.02	2.02
Ratio of net debt to common partners' equity <sup>3</sup>	0.17	0.17	-	-
Increase (decrease) in cash and cash equivalents	11.0	27.8	0.2	(0.8)
– comprised of cash flow from (used in):				
Operating activities	62.6	168.2	42.8	70.0
Financing activities	(0.9)	(58.1)	(49.3)	(27.8)
Investing activities	(50.7)	(82.3)	6.7	(43.0)

### Changes in Financial Position

Operating activities generated \$62.6 million in cash in the fourth quarter, which was a \$19.8 million improvement over same period last year, principally due to significantly higher NBSK pulp prices.

Cash flows from financing activities represent net cash transactions with Canfor prior to the spinout. Prior to the spinout the pulp business operating transactions such as sales of products, and purchases of products and services, were settled in the divisional equity account as they occurred. The excess cash flows of the pulp business were transferred to the central cash management system of Canfor.

The \$50.7 million of cash used in investing activities in the quarter represents \$45.6 million of distributions paid to Canfor and the Fund, with the balance relating to net capital expenditures.

### LIQUIDITY AND FINANCIAL REQUIREMENTS

On November 30, 2006, the Partnership completed a debt financing by private placement of US\$110 million (Cdn \$125.7 million) of unsecured notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013. The proceeds from the issuance of the Notes were used to repay the \$125 million Canfor promissory note. The Partnership also entered into a 3-year \$75 million syndicated unsecured revolving bank credit facility (the Revolving Facility) with \$30.6 million of the Revolving Facility reserved for a letter of credit issued to BC Hydro. The Revolving Facility bears interest and fees at rates that vary depending on the ratio of net debt to operating earnings before interest, taxes, depreciation and amortization (EBITDA) and which may, at the option of the Partnership, be based on lenders' Canadian prime rate, bankers acceptances, US base rate or US LIBOR rate.

Each agreement with respect to the Notes and Revolving Facility contain the same covenants with respect to certain financial ratios and at December 31, 2006 the Partnership was in compliance with all covenants.

### OUTSTANDING UNITS

At February 16, 2007, there were a total of 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.

<sup>3</sup> net debt consists of long-term debt net of cash and cash equivalents

## RISKS AND UNCERTAINTIES

A comprehensive discussion of Risks and Uncertainties was included in the April 28, 2006 Information Circular issued by Canfor and available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com).

In addition, the sensitivity of the Partnership's results to currency fluctuations and price changes for its principal products and input costs, when operating at full capacity, is estimated to be as follows:

(millions of dollars, unaudited)	Impact on annual Net income
Canadian dollar – US \$0.01 change per Canadian dollar	\$ 5
NBSK pulp – US \$10 change per tonne	8
Natural gas cost - \$1 change per gigajoule	4
Chip cost - \$10 change per tonne	24

## SELECTED QUARTERLY PARTNERSHIP FINANCIAL INFORMATION

(unaudited)	Q4 2006	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Q2 2005	Q1 2005
<b>Sales and Income</b> (millions of dollars)								
Sales	<b>229.0</b>	214.3	194.9	196.2	195.9	193.1	198.9	183.3
Operating income (loss)	<b>49.3</b>	49.7	15.7	20.4	16.7	(3.1)	(5.2)	8.3
EBITDA	<b>61.9</b>	62.5	26.8	32.9	29.0	9.1	5.9	19.9
Net income (loss)	<b>44.8</b>	41.9	15.9	20.4	16.6	(3.1)	(5.2)	8.2
<b>Per Partnership unit</b> (dollars) <sup>4</sup>								
Net income (loss), basic and diluted	<b>0.63</b>	0.59	0.22	0.29	0.23	(0.04)	(0.07)	0.12
<b>Statistics</b>								
Pulp shipments (000 mt)	<b>249.8</b>	251.4	244.6	255.7	260.7	257.9	246.8	216.7
Paper shipments (000 mt)	<b>32.8</b>	29.5	31.3	31.0	30.6	31.1	33.0	32.5
Average exchange rate (Cdn\$/US\$) <sup>5</sup>	<b>0.878</b>	0.892	0.891	0.866	0.852	0.832	0.804	0.815
Average NBSK pulp list price – US\$ <sup>6</sup>	<b>730</b>	711	670	622	600	588	613	642

Sales are primarily influenced by changes in market pulp prices, sales volumes and fluctuations in Canadian/US dollar exchange rates. Operating income, net income and EBITDA are primarily impacted by sales and price fluctuations in raw material inputs, energy prices and maintenance costs.

<sup>4</sup> Based on partnership units outstanding at December 31, 2006 (71,270,025) for all periods

<sup>5</sup> Source – Bank of Canada (average noon rate for the period)

<sup>6</sup> Per tonne, delivered to Northern Europe

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

(millions of dollars, unaudited)	3 months ended		6 months ended
	December 31, 2006	September 30, 2006	December 31, 2006
<b>RECONCILIATION OF NET INCOME TO EBITDA</b>			
<b>Net Income</b>	<b>\$ 44.8</b>	<b>41.9</b>	<b>86.7</b>
Add:			
Amortization	12.6	12.8	25.4
Net interest	2.0	1.8	3.8
Foreign exchange loss on long-term debt	2.5	-	2.5
Business acquisition costs and other	-	6.0	6.0
<b>EBITDA (operating income before interest and amortization)</b>	<b>\$ 61.9</b>	<b>62.5</b>	<b>124.4</b>
<b>CALCULATION OF DISTRIBUTABLE CASH</b>			
<b>Cash flow from operating activities</b>	<b>\$ 62.6</b>	<b>37.3</b>	<b>99.9</b>
Change in working capital	1.0	21.8	22.8
Deduct:			
Financing costs	(1.6)	-	(1.6)
Capital expenditures	(5.1)	(6.0)	(11.1)
<b>Distributable cash</b>	<b>\$ 56.9</b>	<b>53.1</b>	<b>110.0</b>
Distributable cash – per partnership unit (in dollars)	\$ 0.80	0.74	1.54
<b>Cash distributions declared (paid and payable)</b>	<b>57.1</b>	<b>31.4</b>	<b>88.5</b>
Cash distributions declared – per partnership unit (in dollars)	\$ 0.80	0.44	1.24

Note: Distributable cash is only presented for the periods subsequent to inception of the Partnership's business on July 1, 2006.

**DISTRIBUTABLE CASH AND CASH DISTRIBUTIONS**

Management determines the level of cash distributions based on the level of cash flow from operations before working capital changes less actual and planned capital expenditures and a reserve for future major capital replacements (estimated at \$4 million per year) less a contingency reserve. During the year distributions are based on estimates of full year cash flow and capital spending and thus distributions may be adjusted as these estimates change. Capital expenditures during 2006, including the second half of the year, were below the level normally expected for the business and as a result the reserve for capital expenditures for the year was increased to provide a reserve for spending in future periods. It is expected that normal seasonal fluctuations in working capital will be funded from a revolving short-term credit facility, and thus will not significantly affect the level of distributions.

Distributions are declared on a monthly basis with record date on the last day of the month and payable within 15 days following. The Partnership began active operation in July 2006, including monthly distributions, and thus there were no distributions in prior periods and no distributions will be paid for earnings from prior periods.

*EBITDA and Distributable cash are not measures determined in accordance with Canadian generally accepted accounting principles and should not be considered as alternatives to net income or cash flow from operations. As there is no standardized method of calculating EBITDA or Distributable cash, the Partnership's use of these terms may not be directly comparable with similarly titled measures used by other companies or income funds.*

## **Additional Information**

Full report to the unitholders, including financial statements, is available on the Partnership's website at [www.canforpulp.com](http://www.canforpulp.com).

The Fund and the Partnership will also hold an analyst call at 8:00 a.m. (PDT) on Monday February 19, 2007 to discuss the fourth quarter results.

The call can be accessed by dialing 416-695-9757 or 1-888-789-0089 (toll free).

The call will be simultaneously webcast at [www.canforpulp.com/investors/webcasts.asp](http://www.canforpulp.com/investors/webcasts.asp)

## **About Canfor Pulp Income Fund**

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

For more information about Canfor Pulp Income Fund and Canfor Pulp Limited Partnership, please visit [www.canforpulp.com](http://www.canforpulp.com).

## **For further information contact:**

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*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, its prospects and uncertainties relating to the Fund 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 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 assumes no obligation to update such information to reflect later events or developments, except as required by law.*

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

<u>(thousands of dollars, except unit and per unit amounts, unaudited)</u>	3 months ended <b>Dec. 31 2006</b>	6 months ended <b>Dec. 31, 2006</b>
<b>Income</b>		
Equity income in Canfor Pulp Limited Partnership	12,169	20,558
<b>Expenses</b>		
Operating expenses (notes 4 & 6)	(15)	-
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<b>Net Income</b>	12,184	20,558
Distributions declared (note 4)	24,147	30,419
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Accumulated distributions in excess of earnings	(11,963)	(9,861)
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<b>Weighted average number of Units</b>	21,641,670	17,947,838
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<b>Net income per unit, basic and diluted</b>	0.56	1.15
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The accompanying notes are an integral part of these interim financial statements.

**Canfor Pulp Income Fund**  
**Consolidated Cash Flow Statements**

(thousands of dollars, unaudited)	3 months ended December 31, 2006	6 months ended December 31, 2006
<b>Cash generated from (used in)</b>		
<b>Operating activities</b>		
Net income	\$ 12,184	20,558
Items not affecting cash:		
Equity income in Canfor Pulp Limited Partnership	(12,169)	(20,558)
Net Change in non-cash working capital	(15)	-
	-	-
<b>Financing activities</b>		
Distributions paid to Unitholders (note 4)	(14,220)	(17,641)
<b>Investing activities</b>		
Distributions received from Canfor Pulp Limited Partnership	14,220	17,641
<b>Beginning, change and ending balance in cash and cash equivalents</b>	<b>\$ -</b>	<b>-</b>

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

**Canfor Pulp Income Fund  
Consolidated Balance Sheet**

**As at  
December 31, 2006**

(thousands of dollars, unaudited)

<b>ASSETS</b>	
<b>Current Assets</b>	
Distributions receivable from Canfor Pulp Limited Partnership	\$ 12,778
<b>Total current assets</b>	<b>12,778</b>
<b>Equity Investment in Canfor Pulp Limited Partnership</b> (note 3)	<b>289,491</b>
	<b>\$ 302,269</b>
<b>LIABILITIES</b>	
<b>Current Liabilities</b>	
Accounts payable (note 6)	\$ 1
Distribution payable (note 4)	12,778
	<b>12,779</b>
<b>UNITHOLDERS' EQUITY</b>	
Unitholders' Equity (note 5)	299,351
Accumulated distributions in excess of earnings – from inception July 1, 2006	(9,861)
	<b>289,490</b>
	<b>\$ 302,269</b>

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

Subsequent events (note 8)

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

Approved by the Trustees

*(signed) Stan Bracken-Horrocks*

*(signed) Charles Jago*

Stan Bracken-Horrocks

Charles Jago

## **Canfor Pulp Income Fund**

### **Notes to the Consolidated Financial Statements as at December 31, 2006.**

#### **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 the Province 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, B.C., 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.

These unaudited interim consolidated financial statements include the accounts of the Fund and the Trust. From the date of its establishment on April 21, 2006 to June 30, 2006 the Fund was inactive. As result there are no comparative figures in the financial statements for any periods prior to the six months ended December 31, 2006.

On July 1, 2006, the Fund completed the indirect acquisition of 20% of the Prince George, B.C. based NBSK pulp and paper business of Canfor Corporation (Canfor). Canfor exchanged 14,254,005 Class A Limited Partnership Units for an equal number of Fund Units, and these units were then distributed by Canfor to its shareholders. As a result of these transactions, on July 1, 2006, Canfor shareholders owned all of the issued and outstanding Fund Units, and the Fund held all issued and outstanding Class A Limited Partnership Units representing a 20% indirect interest in the Partnership.

On November 30, 2006, Canfor exchanged 21,239,537 Class B Exchangeable Limited Partnership Units of the Partnership for the same number of newly issued Fund units and immediately distributed these Fund units to its shareholders as an in-kind taxable dividend of 1.49 units for every 10 Canfor shares held. Following completion of this exchange, there are a total of 35,493,542 Fund units issued and outstanding, and the Fund indirectly holds a total of 35,493,542 units of the Partnership, representing 49.8% of the Partnership. Canfor, through its ownership of Class B Exchangeable Limited Partnership Units, which are indirectly exchangeable for Fund units, owns the remaining 50.2% interest in the Partnership. As a result of the transaction, and the Fund's method of accounting for its investment in the Partnership, the Fund recognized its 20% pro-rata earnings of the Partnership's November income, however, based on the distribution declared by the Partnership on November 30, 2006, the Fund received 49.8% of the total November cash distribution. The Fund has recognized the distribution received in excess of its pro-rata share of the Partnership's income (\$5.1 million or 29.8% of the distribution) as a permanent contribution by Canfor through its ownership in the Partnership.

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.

#### **2. Significant Accounting Policies**

##### *Principles of Consolidation*

The consolidated financial statements include the accounts of the Fund and Canfor Pulp Trust (the "Trust"), its wholly owned holding trust. All significant inter-company transactions have been eliminated.

##### *Investment in Canfor Pulp Limited Partnership*

The Fund accounts for its investment in the Partnership using the equity method. Under the equity method the Fund records its pro rata share of the Partnership's income as an increase in investment. Any distributions declared by the Partnership and accruing to the Fund reduce the carrying value of the Fund's investment in the Partnership.

### *Use of 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 reported in the financial statements and accompanying notes. It is reasonably possible that circumstances may arise that cause actual results to differ from management estimates; however, management does not believe it is likely that such differences will materially affect the Pulp Business' financial position. The valuation of the Fund's investment in the Partnership relative to its market value is the only significant estimate in these financial statements.

### *Net Income per Unit*

Basic net income per Fund unit is based on the weighted average number of Fund units outstanding during the period. At December 31, 2006 the Partnership has 35,776,483 Class B Exchangeable Limited Partnership Units outstanding which can be exchanged for Fund Units at the option of the holder (Canfor). Any issuance of new Fund Units would be accompanied with a corresponding increase in the Fund's investment in the Partnership through the acquisition of Class B Exchangeable Limited Partnership Units. As a result, this potential conversion would not result in any dilution of the Fund's net income per unit.

### *Income taxes*

The Fund is a unit trust for income tax purposes. As such, the Fund is only taxable on any taxable income not allocated to the Unitholders. For the six months ended December 31, 2006, all taxable income of the Fund will be allocated to the Unitholders. Income tax obligations relating to distributions from the Fund are the obligations of the Unitholders.

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

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

(thousands of dollars, unaudited)

Initial investment in the Partnership on July 1, 2006 – 14,254,005 Fund units	\$ 116,560
Issuance of Fund units for exchangeable Partnership units (November 30, 2006) – 21,239,537 Fund units	182,792
Cumulative equity in income of the Partnership	20,558
Cumulative distributions received and receivable	(30,419)
Equity investment in the Partnership as at December 31, 2006	\$ 289,491

The Fund's investment in the Partnership units is recorded using the equity method. The Fund's initial investment in the Partnership at July 1, 2006, represented the Fund's 20% ownership in the transfer of the Pulp and Paper business from Canfor to the Partnership. On November 30, 2006 Canfor exchanged 21,239,537 Class B Exchangeable Limited Partnership Units of the Partnership for the same number of newly issued Fund Units for a total value of \$182.8 million (\$8.61 per unit), representing the Fund's pro rata share of the carrying value of the Partnership units received on the date of the exchange.

#### 4. Distributions

The Fund declared distributions in its first six months of operation as follows:

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

Record Date	Payable Date	Amount per Fund Unit			Amount
		Monthly	Supplemental	Total	
		\$	\$	\$	\$
August 2, 2006	August 15, 2006	0.12	-	0.12	1,710.5
August 31, 2006	September 15, 2006	0.12	-	0.12	1,710.5
September 29, 2006	October 13, 2006	0.12	0.08	0.20	2,850.8
October 31, 2006	November 15, 2006	0.12	0.08	0.20	2,850.8
November 30, 2006	December 15, 2006	0.12	0.12	0.24	8,518.3
December 29, 2006	January 15, 2007	0.14	0.22	0.36	12,777.6
Total		0.74	0.50	1.24	30,418.5

The Fund's monthly distributions are based on the Partnership's monthly distributions. To December 31, 2006, distributions declared by the Fund equaled those declared by the Partnership with the exception of an expense distribution declared by the Partnership totaling \$142,000 payable to the Fund. The expense distribution is accounted for as a recovery of operating expenses and presented on a net basis in the consolidated statement of income and accumulated earnings and distributions. This amount represents the Partnership's commitment to cover the Fund's operating expenses pursuant to the partnership agreement.

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. Unitholders' Equity

The Fund may issue an unlimited number of Fund units for consideration, and on the terms and conditions, determined by the Trustees. Each Fund unit is transferable and represents an equal and undivided beneficial interest in any distributions from the Fund. All Fund units have equal rights and privileges.

On initial distribution on July 1, 2006, the total number of Fund units issued was 14,254,005, equal to the number of Class A Limited Partnership Units for which they were exchanged.

On November 30, 2006, the Fund completed the issuance of 21,239,537 Fund units for a total value of \$182.8 million (\$8.61 per unit) representing the Fund's pro rata share of the carrying value of the Partnership units received on the date of the exchange. Following completion of this exchange, there are a total of 35,493,542 Fund units issued and outstanding.

#### *Redemption Rights*

Fund units are redeemable at any time on demand by the holders thereof upon delivery to the Fund of a duly completed and properly executed notice requesting redemption in a form approved by the Fund Trustees. Upon receipt of the redemption notice by the Fund, all rights with respect to the Fund units tendered for redemption, including the right to receive any distributions which are declared payable to the unitholders of record on a date subsequent to the date of receipt by the Fund of such notice, will be surrendered and the unitholder will be entitled to receive a price per Fund unit equal to the lesser of 90% of the market price of the Fund units as of the date on which the Fund units are surrendered for redemption (Redemption Date); and 100% of the closing market price on the Redemption Date.

### *Exchange Rights*

Canfor holds all remaining (35,776,483) Class B Exchangeable Limited Partnership Units, and it has the ability to indirectly exchange them on a one-for-one basis into Fund units.

### **6. Related Party Transactions**

All accounting, treasury, legal and administrative functions for the Fund are performed on its behalf by the Partnership pursuant to a support agreement. For the three months ended December 31, 2006, the Fund had incurred operating expenses with third parties of \$128,000, compared to \$15,000 for the three-month period ended September 30, 2006. During the fourth quarter the Partnership declared an expense distribution to cover the operating expenses of the Fund as provided for in the Partnership agreement. The expense distribution is accounted for by the fund as a recovery of operating expenses and presented on a net basis in the consolidated statement of income and accumulated earnings and distributions.

### **7. Taxation of Publicly Traded Income Trusts**

Income tax obligations related to the distributions of the Fund are the obligations of the Unitholders.

On October 31, 2006, the Canadian Federal Government announced proposed plans to apply a tax on distributions from publicly traded income trusts, such as the Fund. For existing income trusts the government is proposing a four-year transition period until their 2011 taxation year before the tax would be applicable. The impact to the Fund is unknown at this time and may be material.

### **8. Subsequent Events**

On January 24, 2007 the Fund declared a distribution of \$0.14 per unit or \$5.0 million, payable on February 15, 2007 to unitholders of record on January 31, 2007. On February 16, 2007 the Fund declared a distribution of \$0.14 per unit or \$5.0 million, payable on March 15, 2007 to unitholders of record on February 28, 2007.

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

(millions of dollars, unaudited)	3 months ended December 31,		Year ended December 31,	
	<b>2006</b>	2005	<b>2006</b>	2005
<b>Sales</b>	<b>\$ 229.0</b>	195.9	<b>\$ 834.4</b>	771.2
<b>Costs and expenses</b>				
Manufacturing and product costs	<b>132.5</b>	131.3	<b>512.7</b>	569.6
Freight and other distribution costs	<b>28.3</b>	30.9	<b>114.1</b>	116.0
Amortization	<b>12.6</b>	12.3	<b>49.0</b>	47.2
Selling and administration costs	<b>6.3</b>	4.7	<b>23.5</b>	21.7
	<b>179.7</b>	179.2	<b>699.3</b>	754.5
<b>Operating income</b>	<b>49.3</b>	16.7	<b>135.1</b>	16.7
Business acquisition costs (note 3)	-	-	<b>(5.9)</b>	-
Interest expense, net	<b>(2.0)</b>	-	<b>(3.8)</b>	-
Foreign exchange loss on long term debt	<b>(2.5)</b>	-	<b>(2.5)</b>	-
Other income (expenses)	-	(0.1)	<b>0.1</b>	(0.2)
	<b>(4.5)</b>	(0.1)	<b>(12.1)</b>	(0.2)
<b>Net income</b>	<b>\$ 44.8</b>	16.6	<b>\$ 123.0</b>	16.5
<b>Net income per Partnership unit</b> (in dollars) (note 10)				
Basic and diluted	<b>\$ 0.63</b>	0.23	<b>1.73</b>	0.23
<b>Weighted average Partnership units outstanding</b>	<b>71,270,025</b>	71,270,025	<b>71,270,025</b>	71,270,025
<b>Partners' equity, beginning of period</b>	<b>\$ 593.3</b>	761.4	<b>\$ 728.7</b>	740.0
Issuance of promissory Note on acquisition (notes 3 & 4)	-	-	<b>(125.0)</b>	-
Net transactions with Canfor (note 1)	-	(49.3)	<b>(57.2)</b>	(27.8)
Net income for the period	<b>44.8</b>	16.6	<b>123.0</b>	16.5
Distributions to partners (notes 13 & 16)	<b>(57.1)</b>	-	<b>(88.5)</b>	-
<b>Partners' equity, end of period</b>	<b>\$ 581.0</b>	728.7	<b>\$ 581.0</b>	728.7

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

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

(millions of dollars, unaudited)	3 months ended December 31,		Year ended December 31,	
	2006	2005	2006	2005
<b>Cash and cash equivalents generated from (used in)</b>				
<b>Operating activities</b>				
Net income	\$ 44.8	16.6	\$ 123.0	16.5
Items not affecting cash:				
Amortization	12.6	12.3	49.0	47.2
Unrealized foreign exchange loss on long term debt	2.5	-	2.5	-
Employee future benefits	1.5	1.9	7.5	4.2
Other	2.2	-	(3.3)	-
Cash flow from operations before working capital changes	63.6	30.8	178.7	67.9
Changes in non-cash working capital (note 12)	(1.0)	12.0	(10.5)	2.1
	62.6	42.8	168.2	70.0
<b>Financing activities</b>				
Repayment of promissory note	(125.0)	-	(125.0)	-
Proceeds of long-term debt	125.7	-	125.7	-
Financing costs	(1.6)	-	(1.6)	-
Net transactions with Canfor	-	(49.3)	(57.2)	(27.8)
	(0.9)	(49.3)	(58.1)	(27.8)
<b>Investing activities</b>				
Property, plant and equipment, net	(5.1)	6.6	(19.6)	(43.0)
Distributions paid to partners (note 13)	(45.6)	-	(62.7)	-
Other	-	0.1	-	-
	(50.7)	6.7	(82.3)	(43.0)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>11.0</b>	<b>0.2</b>	<b>27.8</b>	<b>(0.8)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>17.4</b>	<b>0.4</b>	<b>0.6</b>	<b>1.4</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 28.4</b>	<b>0.6</b>	<b>\$ 28.4</b>	<b>0.6</b>
<b>Cash payments in the period</b>				
Interest, net	\$ 1.2	-	\$ 2.4	-

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

**Canfor Pulp Limited Partnership  
Consolidated Balance Sheets**

(millions of dollars, unaudited)	As at December 31, 2006	As at December 31, 2005
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 28.4	\$ 0.6
Accounts receivable (note 9)		
Trade	130.9	127.9
Other	6.7	10.0
Inventories (note 6)	111.0	107.0
Prepaid expenses	13.1	4.9
<b>Total current assets</b>	<b>290.1</b>	250.4
<b>Property, plant and equipment</b> (note 8)	<b>598.6</b>	627.9
<b>Deferred charges</b>	<b>4.7</b>	0.1
	<b>\$ 893.4</b>	\$ 878.4
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 9)	\$ 125.5	\$ 124.0
Distributions payable (note 13)	25.8	-
<b>Total current liabilities</b>	<b>151.3</b>	124.0
<b>Long-term debt</b> (note 4)	<b>128.2</b>	-
<b>Long-term accruals and liabilities</b> (note 5)	<b>32.9</b>	25.7
	<b>\$ 312.4</b>	\$ 149.7
<b>PARTNERS' EQUITY</b>		
Capital – 14,254,005 Class A Limited Partnership Units and 57,016,020 Class B Limited Partnership Units (notes 1 & 3)	<b>581.0</b>	728.7
<b>Total Partners' Equity</b>	<b>581.0</b>	728.7
	<b>\$ 893.4</b>	\$ 878.4

Commitments and contingencies (note 14)

Subsequent events (note 16)

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

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

(signed) Stan Bracken-Horrocks

Stan Bracken-Horrocks  
Director

(signed) Paul Richards

Paul Richards  
Director

## **Canfor Pulp Limited Partnership**

### **Notes to the Consolidated Financial Statements as at December 31, 2006 and 2005**

#### **1. Business Description and Basis of Presentation**

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).

On July 1, 2006, Canfor transferred the Pulp Business to the Partnership in exchange for a \$125 million promissory note, 14,254,005 Class A Limited Partnership Units and 57,016,020 Class B Exchangeable Limited Partnership Units (the Spinout). Canfor then exchanged its Class A Limited Partnership Units for equal number of Units of Canfor Pulp Income Fund (the Fund). Finally Canfor distributed to its shareholders, for each Canfor share held by them, one New Common Share of Canfor and 0.1 of a Unit of the Fund (Fund Unit), with the distribution of the Fund Units being structured as a return of capital on the Canfor Shares. As a result, on the date of the spinout, Canfor shareholders owned all of the issued and outstanding Fund Units, with the outstanding Fund Units representing a 20% indirect interest in the Partnership and thus the Pulp Business. On November 30, 2006 Canfor exercised its right to exchange Class B Exchangeable Limited Partnership Units for Fund Units and 21,239,537 units were exchanged. The exchange was made in order to provide Canfor with the Fund Units necessary to enable it to pay a dividend-in-kind to its shareholders. Following completion of this exchange Canfor owns 50.2% and the Fund indirectly owns 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.

All pulp produced by the Pulp Business is sold by the Pulp Business' sales and marketing group to customers primarily in North America, Europe and Asia. The kraft paper produced by the Pulp Business is sold by a 50% owned general partnership to customers in North America and Europe.

For all periods ending prior to July 1, 2006, these financial statements present the financial position, results of operations, and cash flows of the Pulp Business on a carve out basis from Canfor as if operated as a stand-alone partnership entity subject to Canfor control. As a result, the transaction has been accounted for as a continuity of interests. The accompanying financial statements include allocations of certain of Canfor's assets, liabilities and costs. The financial condition, results of operations, and cash flows of the Pulp Business for these comparative periods are not necessarily indicative of the financial condition, results of operations or cash flows that would have been incurred if the Pulp Business was a separate legal entity. Prior to July 1, 2006, the Pulp Business did not operate bank accounts independent or separate from Canfor (other than for marketing subsidiaries) and, as a result and for purposes of prior periods, the combined effect of all transactions is reflected in the net transactions with Canfor line in the Partners' equity.

The statements of income for all periods prior to July 1, 2006, include selling and administration expenses of the Pulp Business, as historically reported in Canfor's financial statements, that have been allocated to the Pulp Business based on specific identification and, where specific identification has been deemed impractical, on a basis which management believes reasonably reflects the cost of services provided. Employee benefits, consisting of such costs as pension, health and welfare and payroll taxes are based on a percentage of actual payroll or allocated payroll charges to the Pulp Business. Amortization is based upon specific identification of the assets utilized in the Pulp Business. Allocated corporate expenses have been charged to the Pulp Business based on specific identification or, when this is deemed impractical, on a basis that management believes reasonably reflects the cost of services provided. Management believes these expense allocations adequately reflect the estimated cost of services provided but may not necessarily be indicative of actual costs that would have been incurred if Canfor had not provided these services.

The balance sheet at December 31, 2005, includes all assets and liabilities directly attributable to the Pulp Business including an allocation of certain of Canfor's corporate assets and liabilities. Employee future benefit liabilities include the obligations for health care and other non-pension benefits for the active salaried employees and active and retired hourly employees of the Pulp Business. The Pulp Business participated in the centralized cash management systems of Canfor, and as a result, did not have separate bank accounts, except for cash held in international marketing operations.

These 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.

#### *Economic Dependence*

The Partnership depends on Canfor to provide approximately 65% of its fibre supply as well as to provide certain key business and administrative services as described in note 9. As a result of these relationships as well as other relationships described throughout these financial statements, the Partnership considers its operations to be dependent on its ongoing relationship with Canfor.

## **2. Significant Accounting Policies**

These interim financial statements do not include all of the note disclosures required by Canadian generally accepted accounting principles for annual financial statements and, accordingly, should be read in conjunction with the Pulp Business' annual financial statements and notes included in the April 28, 2006, Canfor Information Circular, available at [www.canforpulp.com](http://www.canforpulp.com) or [www.sedar.com](http://www.sedar.com).

The unaudited interim financial statements for the period ended December 31, 2006, including comparative periods, reflects the current activities of the Pulp Business and the Partnership and have been prepared based on the most recent information available to management.

#### *Principles of Consolidation*

These consolidated financial statements include the accounts of the Partnership, its wholly owned subsidiaries and its 50% interests in Premium One Papers (a partnership) and Canfor April Corporation (a joint venture). The 50% interests in the partnership and joint venture are accounted for using proportionate consolidation. All significant inter-company transactions have been eliminated.

#### *Cash and Cash Equivalents*

Cash and cash equivalents include cash on hand and highly liquid investments with an original maturity date of 90 days or less.

### 3. Business Acquisition Costs and Partners' Equity

The Partnership incurred costs related to its initial organization and the acquisition of the Pulp Business from Canfor principally comprised of legal, accounting, audit and consulting fees.

Prior to the transfer, the net value of the Pulp Business is reflected in Partners' Equity. On July 1, 2006, the Pulp Business was transferred to the Partnership at Canfor's net book value as follows:

Net assets transferred (millions of dollars, unaudited)	
Non cash working capital	124.7
Property plant and equipment	612.9
Other accruals and liabilities	(29.8)
	<hr/> 707.8
Consideration provided	
Promissory note	125.0
Partners' equity	582.8
	<hr/> 707.8

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

On November 30, 2006, the Partnership completed a debt financing by private placement of US\$110 million (Cdn \$125.7 million) of unsecured notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013. The proceeds from the issuance of the Notes were used to repay the \$125 million Canfor promissory note.

The Partnership also entered into a 3-year \$75 million syndicated unsecured revolving bank credit facility (the Revolving Facility) with \$30.6 million of the Revolving Facility reserved for a standby letter of credit issued to BC Hydro (note 14). The Revolving Facility bears interest and fees at rates that vary depending on the ratio of net debt to operating earnings before interest, taxes, depreciation and amortization (EBITDA) and which may, at the option of the Partnership, be based on lenders' Canadian prime rate, bankers acceptances, US base rate or US LIBOR rate.

The agreements relative to the Notes and Revolving Facility contain the same covenants with respect to certain financial ratios and at December 31, 2006, the Partnership was in compliance with all covenants.

The fair value of long-term debt at December 31, 2006 was \$ 127.4 million (US\$109.3 million).

### 5. Long-term Accruals and Liabilities

(millions of dollars, unaudited)	December 31, 2006	December 31, 2005
Accrued pension obligations	2.7	0.9
Post employment benefits	30.2	24.8
	<hr/> 32.9	<hr/> 25.7

## 6. Inventories

(millions of dollars, unaudited)	December 31, 2006	December 31, 2005
Pulp	48.9	42.2
Paper	11.6	11.4
Wood chips	5.4	9.0
Processing materials and supplies	45.1	44.4
	<b>111.0</b>	107.0

## 7. 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)	3 months ended December 31		12 months ended December 31	
	2006	2005	2006	2005
Pension plans	1.0	1.2	4.4	4.7
Other employee future benefit plans	1.5	1.0	6.1	4.9
Contributions to forest industry union plans	1.2	1.2	6.2	6.3
	<b>3.7</b>	3.4	<b>16.7</b>	15.9

## 8. Property Plant and Equipment

(millions of dollars, unaudited)	December 31, 2006		
	Cost	Accumulated amortization	Net
Land	5.4	-	5.4
Buildings, machinery and equipment	1,272.6	684.5	588.1
Construction in progress	5.1	-	5.1
	<b>1,283.1</b>	<b>684.5</b>	<b>598.6</b>

(millions of dollars, unaudited)	December 31, 2005		
	Cost	Accumulated amortization	Net
Land	5.2	-	5.2
Buildings, machinery and equipment	1,248.7	629.3	619.4
Construction in progress	3.3	-	3.3
	1,257.2	629.3	627.9

## 9. Related Party Transactions

The Partnership's transactions with related parties are based on agreed upon amounts, unless otherwise noted below.

The Partnership purchased wood chips and hog fuel from Canfor sawmills in the amount of \$27.1 million for the three months ended December 31, 2006 (2005 — \$15.7 million) and \$83.3 million for the twelve months ended December

31, 2006 (2005 — \$106.2 million). The Partnership also purchased wood chips from Lakeland Mills Ltd. and Winton Global Lumber Ltd., in which Canfor owns a one-third interest. Purchases from these entities for the three months ended December 31, 2006 were \$2.7 million (2005 — \$1.9 million) and for the twelve months ended December 31, 2006, \$8.6 million (2005 — \$11.1 million).

Effective July 1, 2006, the Partnership entered into a services agreement under which Canfor provides certain business and administrative services to the Partnership. Total value of the services provided in the three months ended December 31, 2006 was \$1.4 million (2005— \$2.9 million) and for the twelve months ended December 31, 2006 was \$8.5 million (2005— \$11.6 million). The corporate costs in comparative periods prior to the acquisition were based on estimates of the Pulp Business' share of Canfor's corporate costs (Note 1).

Effective July 1, 2006, the Partnership entered into an incidental services agreement with Canfor, under which the Partnership provides certain business and administrative services to Canfor. Total value of the services provided in the three months ended December 31, 2006 was \$0.4 million (2005— \$0.4 million) and for the twelve months ended December 31, 2006 was \$1.5 million (2005— \$1.5 million).

The Partnership markets bleached chemi-thermo mechanical pulp production from Canfor's Taylor Pulp Mill for which it earned commissions totaling \$0.3 million for the three months ended December 31, 2006 (2005 — \$0.7 million) and \$2.3 million for the twelve months ended December 31, 2006 (2005— \$2.8 million). The Partnership also purchased chemi-thermo mechanical pulp from the Canfor Taylor Pulp Mill for resale totaling \$2.3 million for the three months ended December 31, 2006 (2005 — \$2.1 million) and \$10.1 million for the twelve months ended December 31, 2006 (2005 — \$8.0 million). In respect of the products marketed and services provided for the Canfor Taylor Pulp Mill, the partnership held balances of \$6.3 million in accounts receivable - trade and \$6.6 million in accounts payable to Canfor at December 31, 2006 (2005 — \$8.8 million accounts receivable - trade and \$9.8 million in accounts payable to Canfor).

The Partnership markets the NBSK pulp produced by Howe Sound Pulp and Paper Limited Partnership (HSLP), a partnership 50% owned by Canfor, for which it earned commissions totaling \$0.7 million for the three months ended December 31, 2006 (2005 — \$1.5 million) and \$4.7 million for the twelve months ended December 31, 2006 (2005 — \$6.0 million). In respect of the products marketed and service provided for HSLP, the partnership held balances of \$31.9 million in accounts receivable - trade and \$23.1 million in accounts payable to HSLP at December 31, 2006 (2005 — \$32.3 million in accounts receivable - trade and \$35.6 million in accounts payable to HSLP).

On July 1, 2006, Canfor transferred the Pulp Business to the Partnership in exchange for a \$125 million promissory note, 14.254 million Class A Limited Partnership Units and 57.016 million Class B Exchangeable Limited Partnership Units. The Partnership repaid the debt in full on November 30, 2006. For the three months ended December 31, 2006, total interest paid or payable to Canfor was \$1.6 million and for the six months ended December 31, 2006, was \$3.7 million.

At December 31, 2006, a total of \$14.3 million was outstanding as accounts payable to Canfor in respect of purchases of wood chips, hog fuel, services and amounts paid on behalf of the Partnership. At December 31, 2006, a total of \$0.8 million was payable to Lakeland Mills Ltd. and Winton Global Lumber Ltd. for wood chips (2005 - \$0.7 million).

During the three months ended December 31, 2006, the Partnership declared distributions totaling \$57.1 million to its limited partners. Distributions to Canfor were \$32.9 million, of which \$20.0 million was paid, with the balance of \$12.9 million payable on December 31, 2006. Distributions to the Fund were \$24.2 million, of which \$11.3 million was paid, with the balance of \$12.9 million payable on December 31, 2006.

#### **10. Income per Partnership Unit**

Basic income 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. For purposes of comparative amounts for periods prior to July 1, 2006, it was assumed that the same number of units was outstanding throughout the comparative periods. There were no other securities with rights to conversion into Partnership units outstanding.

## 11. Financial Instruments

The Partnership uses a variety of financial instruments to reduce its exposure to risks associated with fluctuations in foreign currency exchange rates, pulp prices and energy costs.

At December 31, 2006, the Partnership had outstanding pulp swaps to hedge 7,500 tonnes (2,500 tonnes per month to March 2007) of future pulp sales at an average price of US\$683 per tonne, along with matching US dollar forward contracts for the exchange of US\$5.1 million at an average rate to 1.1092. There was a combined unrealized loss of \$1.0 million on the pulp swaps and forward contracts at the end of the period.

At December 31, 2006, the Partnership had outstanding commodity swaps hedging future natural gas purchases of 3.6 million gigajoules extending to October 2009 with an unrealized loss of \$0.8 million.

## 12. Changes in Non-Cash Working Capital

(millions of dollars, unaudited)	3 months ended December 31,		12 months ended December 31,	
	2006	2005	2006	2005
Accounts receivable	23.9	(3.4)	0.3	2.1
Inventories	(11.2)	4.4	(4.0)	7.3
Prepaid expenses	4.2	2.5	(8.2)	1.3
Accounts payable and accrued liabilities	(17.9)	8.5	1.4	(8.6)
	(1.0)	12.0	(10.5)	2.1

## 13. Distributions

The Partnership declared distributions in its first six months of operation as follows:

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

Record Date	Payable Date	Amount per Partnership Unit			Amount
		Monthly	Supplemental	Total	
		\$	\$	\$	\$
August 2, 2006	August 15, 2006	0.12	-	0.12	8.5
August 31, 2006	September 15, 2006	0.12	-	0.12	8.5
September 29, 2006	October 13, 2006	0.12	0.08	0.20	14.3
October 31, 2006	November 15, 2006	0.12	0.08	0.20	14.3
November 30, 2006	December 15, 2006	0.12	0.12	0.24	17.1
December 29, 2006	January 15, 2007	0.14	0.22	0.36	25.8
Total		0.74	0.50	1.24	88.5

## 14. Commitments and Contingencies

In 2003, Canfor entered into an agreement with BC Hydro to build an electrical cogeneration facility at the Prince George Pulp and Paper Mill. Under the agreement, BC Hydro contributed \$45.8 million of the project costs, with Canfor contributing the balance. The agreement was assigned to the Partnership effective July 1, 2006, with incentive payments totaling \$11.4 million outstanding. The final incentive payment of \$11.4 million was received August 9, 2006 and transferred to Canfor. The total incentive payments of \$45.8 million were accounted for as a credit to property, plant and equipment of the Partnership. The project was completed in the second quarter of 2005 at a net cost to the Pulp Business of \$69.6 million. The agreement entails a 15 year commitment with BC Hydro for power displacement at the cogeneration facility, whereby a proportionate repayment is required should the facility not generate the minimum of 390 gigawatt hours of electricity per year. Under the agreement, the Partnership is required to post a letter of credit as security in annually decreasing amounts as minimum required amount of electricity is generated. As of December 31, 2006, the Partnership has no repayment obligation under the terms of the agreement and a standby letter of credit in the amount \$30.6 million was issued to BC Hydro.

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

(millions of dollars, unaudited)	Pulp	Paper	Unallocated Costs <sup>(d)</sup>	Total
<b>3 months ended December 31, 2006</b>				
<b>Sales to external customers</b>	<b>197.6</b>	<b>31.4</b>	<b>-</b>	<b>229.0</b>
<b>Sales of pulp to paper segment <sup>(c)</sup></b>	<b>20.1</b>	<b>(20.1)</b>	<b>-</b>	<b>-</b>
<b>Operating income (loss)</b>	<b>50.6</b>	<b>2.6</b>	<b>(3.9)</b>	<b>49.3</b>
<b>Amortization</b>	<b>11.5</b>	<b>1.0</b>	<b>0.1</b>	<b>12.6</b>
<b>Capital expenditures</b>	<b>4.5</b>	<b>0.6</b>	<b>-</b>	<b>5.1</b>
<b>3 months ended December 31, 2005</b>				
Sales to external customers	168.2	27.7	-	195.9
Sales of pulp to paper segment <sup>(c)</sup>	15.6	(15.6)	-	-
Operating income (loss)	18.5	1.7	(3.5)	16.7
Amortization	11.3	1.0	-	12.3
Capital expenditures	(6.7)	0.1	-	(6.6)
<b>Year ended December 31, 2006</b>				
<b>Sales to external customers <sup>(b)</sup></b>	<b>720.9</b>	<b>113.5</b>	<b>-</b>	<b>834.4</b>
<b>Sales of pulp to paper segment <sup>(c)</sup></b>	<b>71.4</b>	<b>(71.4)</b>	<b>-</b>	<b>-</b>
<b>Operating income (loss)</b>	<b>146.3</b>	<b>3.2</b>	<b>(14.4)</b>	<b>135.1</b>
<b>Amortization</b>	<b>45.0</b>	<b>3.8</b>	<b>0.2</b>	<b>49.0</b>
<b>Capital expenditures</b>	<b>16.9</b>	<b>0.8</b>	<b>1.9</b>	<b>19.6</b>
<b>Identifiable assets</b>	<b>784.2</b>	<b>70.8</b>	<b>38.4</b>	<b>893.4</b>
<b>Year ended December 31, 2005</b>				
Sales to external customers <sup>(b)</sup>	653.8	117.4	-	771.2
Sales to other segments <sup>(c)</sup>	65.6	(65.6)	-	-
Operating income (loss)	26.7	3.6	(13.6)	16.7
Amortization	43.4	3.8	-	47.2
Capital expenditures	42.1	0.3	0.6	43.0
Identifiable assets	797.6	77.9	2.9	878.4

(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 United States representing 43% (2005 – 40%).

(b) Sales to two largest customers represented approximately 34% of pulp segment sales (2005 – 37%).

(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. (d) Unallocated costs represent actual head office administrative costs in the third and fourth quarters of 2006. For all periods prior to July 1, 2006, head office administrative costs were based on allocated Canfor corporate expenses as described in Note 1.

## 16. Subsequent Events

On January 24, 2007 the Partnership declared a distribution of \$0.14 per unit or \$10.0 million, payable on February 15, 2007 to unitholders of record on January 31, 2007. On February 16, 2007, the Partnership declared a distribution of \$0.14 per unit or \$10.0 million, payable on March 15, 2007 to unitholders of record on February 28, 2007.