

Western Forest Products Inc.

2011 First Quarter Report

May 9, 2011

To our Shareholders,

We continued to make positive strides in the first quarter of 2011. Our improvements have led to better financial results which were achieved despite the continued strengthening of the Canadian dollar:

- Positive EBITDA of \$8.2 million in the quarter
- Liquidity of \$95.2 million compared to \$54.5 million a year ago
- Net debt to capitalization reduced to 12% from 30% a year ago
- Sales revenues increased 31% over the first quarter last year
- Sales volumes of all our major product segments increased over last year
- Operating cash flow generated \$35.1 million in the quarter

As a result of the cash generated from operations and sales of non-core assets made in the first quarter of 2011, our balance sheet continues to strengthen.

Our return to profitability continues to come largely as a result of operational initiatives including:

- Operating cost reductions and inventory control
- Refocused marketing and refined product mix to increase sales value
- Improvement in our sales and marketing infrastructure and overall management of our balance sheet

These results were achieved in a tough North American market environment, with a Canadian dollar that was 5% stronger than the US dollar compared to the same quarter last year. Shipments of our lumber products to Japan and China continue to grow and more than offset weak market demand for lumber products in the US. We continue to look for alternative markets, including Asia.

In addition to continued challenging markets, we have had poor weather over the early part of the year, resulting in some log supply shortages. Harsh weather conditions at the end of the first quarter impacted our ability to log, particularly in higher elevation operating areas. This will result in continued log supply issues in the second quarter which we are working to offset.

As we move forward through 2011, Western is in a much stronger position, which will allow us to shift focus to longer term strategic initiatives. We will pursue quick-return capital re-investment opportunities in 2011 to further improve our cost position.

Our priorities for 2011 follow:

- Continue to enhance our safety programs to achieve our ultimate objective of a zero medical incident rate
- Increase market share with our key customers in our core product segments.
- Increase our logging activity by one third
- Continue to expand lumber production to meet market demand.
- Institutionalize our margin improvement and cost reduction programs
- Begin the first phase of our \$125 million capital investment program

We are not as yet where we need to be, and there is more work to be done. That said, we have shown that we can deliver positive results even in a difficult market environment. We at Western are optimistic about our future.

I look forward to reporting our progress throughout this year.



Dominic Gammiero
Chairman and CEO



Lee Doney
Vice-Chairman

Management's Discussion & Analysis

The following discussion and analysis reports and comments on the financial condition and results of operations of Western Forest Products Inc. (the "Company", "Western", "us", "we", or "our"), on a consolidated basis, for the three months ended March 31, 2011 to help security holders and other readers understand our Company and the key factors underlying our financial results. This discussion and analysis should be read in conjunction with the unaudited condensed consolidated interim financial statements for the period and with the audited annual consolidated financial statements and management's discussion and analysis ("MD&A") for the year ended December 31, 2010 (the "2010 Annual Report"), all of which can be found on the System for Electronic Document Analysis and Retrieval ("SEDAR"), at <http://www.sedar.com>.

The Company has prepared these unaudited condensed consolidated interim financial statements in accordance with International Financial Reporting Standards ("IFRS") applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting*, and IFRS 1, *First-Time Adoption of IFRS*. For comparative purposes all financial statement amounts related to the three month period ended March 31, 2010 and the year ended December 31, 2010 have been restated in accordance with IFRS.

Reference is also made to EBITDA¹. EBITDA is defined as operating income (loss) prior to operating restructuring costs and other income (expenses), plus depreciation of property, plant and equipment, amortization of intangible assets, the reversal of impairments of intangible assets, and the change in fair value adjustments to biological assets. Western uses EBITDA as a benchmark measurement of our own operating results and as a benchmark relative to our competitors. We consider EBITDA to be a meaningful supplement to operating income as a performance measure primarily because amortization expense, impairments, reversals of impairments and changes in the fair value of biological assets are non-cash costs, and vary widely from company to company in a manner that we consider largely independent of the underlying cost efficiency of their operating facilities. Further, operating restructuring costs are not expected to occur on a regular basis and may make comparisons of our operating results between periods more difficult. We also believe EBITDA is commonly used by securities analysts, investors and other interested parties to evaluate our financial performance.

EBITDA does not represent cash generated from operations as defined by IFRS and it is not necessarily indicative of cash available to fund cash needs. Furthermore, EBITDA does not reflect the impact of a number of items that affect our net income (loss). EBITDA is not a measure of financial performance under IFRS, and should not be considered as an alternative to measures of performance under IFRS. Moreover, because all companies do not calculate EBITDA in the same manner, EBITDA as calculated by Western may differ from EBITDA as calculated by other companies.

This management's discussion and analysis contains statements which constitute forward-looking statements and forward-looking information within the meaning of applicable securities laws. Those statements and information appear in a number of places in this document and include statements and information regarding our current intent, belief or expectations primarily with respect to market and general economic conditions, future costs, expenditures, available harvest levels and our future operating performance, objectives and strategies. Such statements and information may be indicated by words such as "estimate", "expect", "anticipate", "plan", "intend", "believe", "should", "may" and similar words and phrases. Readers are cautioned that it would be unreasonable to rely on any such forward-looking statements and information as creating any legal rights, and that the statements and information are not guarantees and may involve known and unknown risks and uncertainties, and that actual results and objectives and strategies may differ or change from those expressed or implied in the forward-looking statements or information as a result of various factors. Such risks and uncertainties include, among others: general economic conditions, competition and selling prices, changes in foreign currency exchange rates, labour disruptions, natural disasters, relations with First Nations groups, changes in laws, regulations or public policy, misjudgments in the course of preparing forward-looking statements or information, changes in opportunities and other factors referenced under the "Risk Factors" section in the MD&A in our 2010 annual report, and those referenced in the MD&A in this quarterly report. All written and oral forward-looking statements or information attributable to us or persons acting on our behalf are expressly qualified in their entirety by the foregoing cautionary statements. Except as required by law, Western does not expect to update forward-looking statements or information as conditions change.

¹ Earnings Before Interest, Tax, Depreciation and Amortization

Unless otherwise noted, the information in this discussion and analysis is updated to May 9, 2011. Certain prior period comparative figures may have been reclassified to conform to the current period's presentation. All financial references are in millions of Canadian dollars unless otherwise noted.

Summary of Selected Quarterly Results¹

	Three months ended March 31,	
	2011	2010
<i>(millions of dollars except where noted)</i>		
Sales	\$ 180.8	\$ 138.3
EBITDA	8.2	9.3
EBITDA as % of sales	4.5%	6.7%
Operating income before restructuring items and other income (expenses)	2.0	2.7
Net income (loss) from continuing operations	(0.7)	9.7
Net income (loss)	(1.0)	9.1
Basic and diluted net income (loss) per share (dollars)	\$ -	\$ 0.02

⁽¹⁾ Included in Appendix A is a table of selected results for the last eight quarters.

Overview

Despite challenging market conditions, Western was again able to generate a positive EBITDA in the quarter. Product demand in most of the Company's markets has strengthened, but still remains well below historical trend levels. Current indications are that the US housing market will take longer to recover than had earlier been anticipated. Also contributing to the challenging operating environment has been the negative impact on our revenues of the continuing increase in the strength of the Canadian dollar relative to the US dollar. The average exchange rate for the first quarter of 2011 was 0.986 (which is the highest quarterly average rate since the fourth quarter of 2007) and is 5% higher than the average of 1.040 in the first quarter of 2010. Our focus continues to be on reducing costs and enhancing the operating efficiencies of all of our activities, while further strengthening our balance sheet.

The net loss for the first quarter of 2011 was \$1.0 million, which is a decline from the net income of \$9.1 million reported a year earlier, and a decline of \$21.1 million compared to the previous quarter. The first quarter of 2010 results benefited from the inclusion of a net \$8.9 million one-time gain that arose from the reorganization of WFP Forest Products Limited. Excluding this item, the net loss of \$1.0 million for the first quarter of 2011 is similar to the 2010 result. The fourth quarter of 2010 includes a net gain of \$15.8 million, being primarily the reversal of impairments on our crown timber tenures and the change in fair value of our biological assets which was required as a result of our transition to reporting under IFRS. Excluding this item, the net income for the first quarter of 2011 was \$5.3 million below the previous quarter.

In the first quarter of 2011 Western reported EBITDA of \$8.2 million compared to \$9.3 million for the same period a year earlier and \$5.8 million in the fourth quarter of 2010. Our cash position increased to \$28.7 million at the end of the first quarter of 2011, primarily as a result of cash generated from operations and reductions in inventories.

On February 11, 2011, the Company completed the sale of certain non-core properties to TimberWest Forest Corp. for a purchase price of \$21.9 million. The sale included properties located in the southern portion of Vancouver Island, near Jordan River. These properties, which encompass approximately 7,678 hectares, are situated in the land districts of Renfrew and Malahat. The net proceeds from the sale were used to pay down the Company's long-term debt in accordance with its lending agreements. A net loss on the disposal of \$1.1 million was recognized in the first quarter of 2011.

Operating Results

EBITDA of \$8.2 million reported for the first quarter of 2011 was marginally lower than the \$9.3 million reported in the same quarter last year, and a \$2.4 million improvement over the \$5.8 million earned in the fourth quarter of 2010. The EBITDA result for the first quarter of 2011 reflects increased operating levels, higher sales volumes and prices for most products and a more favorable mix of sales compared to the first quarter of 2010. However, these positive variances were offset by a negative impact of foreign exchange, increased cost of sales, higher freight costs and higher selling and administrative expenses in the current quarter.

The operating results for the first quarter of 2011 incorporated shutdown costs that were \$3.8 million less than those incurred in 2010, as production was increased to meet demand. Lumber production was 15% higher in the first quarter of 2011 compared to the first quarter of 2010 and our sawmills operated at 78% of capacity in the first quarter of 2011 compared to 56% of capacity in the same quarter of 2010. The majority of this increase in operating capacity related to the Nanaimo mill which ran for the first quarter of 2011, but was idle in the same quarter in 2010 and the Ladysmith mill which ran at approximately 70% of capacity during the quarter but was also idle in the first quarter of 2010. Demand for logs in the first quarter of 2011 was relatively strong, whereas log production was 2% lower in the first quarter of 2011 as weather related issues, particularly in March, hampered production.

As previously mentioned, our operating results were negatively impacted by an approximate 5% strengthening in the value of the Canadian dollar relative to the US dollar from the first quarter of 2010, which reduced our Canadian dollar proceeds received on US dollar denominated sales.

Sales

(millions of dollars)

	Three months ended March 31,	
	2011	2010
Lumber	\$ 129.0	\$ 102.2
Logs	36.3	24.5
By-products	15.5	11.6
Total sales	<u>\$ 180.8</u>	<u>\$ 138.3</u>

Total sales dollars increased by 31% in the first quarter of 2011 compared to 2010 due primarily to increased volumes of shipments. The negative effect of the stronger Canadian dollar on revenues in the current quarter tempered this increase.

Lumber sales revenues increased by 26% when compared to the first quarter of 2010 primarily because of higher shipment volumes. Lumber shipments increased by 24% to 183 million board feet in the first quarter of 2011. Average lumber prices realized were marginally higher in the current quarter at \$705 per thousand board feet, compared to \$695 in the first quarter of 2010. Lumber sales values in the first quarter of 2011 have seen modest price increases in all major product categories, particularly whitewood products, when compared to the same period last year. In the first quarter of 2011, 29% of lumber sales were made to China compared to 22% in the same period in 2010.

Log sales revenues in the first quarter of 2011 increased by 48% compared to the same period last year. The increase is due to a 22% increase in the volume of logs sold and average log prices realized in the first quarter of 2011 being 15%, or \$9 per cubic metre, higher than a year ago. Overall log demand for the quarter was strong, relative to prior quarters. Increases in volumes sold were achieved in our peeler and shingle log sales in North American markets as well as sales to Korea and China. Domestic log prices, with the exception of cedar sawlogs, have generally increased since the first quarter of 2010 as a result of a strong pulplug market and supply shortages for most log species. The volume of pulplug sales was lower in the current quarter which reflects a reduced supply of log volume from both internal and external sources. The increase in the overall average log price realized is partly because of higher export prices, combined with a higher value mix of logs sold domestically.

By-product revenues increased by \$3.9 million, or 34%, in the current quarter compared to the first quarter of 2010, mainly because of increased chip production and higher chip prices. Chip production in the first quarter of 2011 increased by 25% over 2010 largely due to increased sawmill production. Chip prices were approximately 10% higher, which is a result of higher pulp mill net realizations which drive the chip pricing formula used in our fibre agreements with certain customers.

Total freight costs were \$21.1 million in the first quarter of 2011, which compared to the first quarter of 2010 cost of \$13.6 million. Shipment volumes of lumber were higher in the current quarter which accounts for approximately \$3.5 million of the increase. The balance of the increase results from an increased proportion of our shipments being made to China in 2011 which incur relatively more costly ocean freight, and also the impact of rising oil prices on general freight rates.

Selling and administration costs increased by \$1.2 million to \$6.6 million in the current quarter compared to \$5.4 million in the first quarter of 2010, primarily because of increased salary costs. The increase in salary costs results from the re-instatement of base salaries following the reductions taken in June 2009, and also the inclusion of performance-based bonus accruals expected for this year. Finance costs decreased from \$3.2 million in the first quarter of 2010 to \$1.9 million in the current quarter. This decrease is primarily attributable to a reduction in the outstanding debt amount over the respective periods which resulted from the proceeds of non-core asset sales being used to pay down debt subsequent to March 31, 2010. Also contributing to this reduction is the benefit of lower interest rates negotiated in the amendments to the loan agreements effected in late December 2010.

Other expenses of \$0.5 million for the first quarter of 2011 comprised net losses on non-core asset sales of \$0.8 million, a gain on the sale of an equity interest in certain real estate properties of \$2.4 million (for further details see *Related Parties* on page 8), an expense incurred of \$2.5 million to amend the terms of certain contractual arrangements, and other items totaling income of \$0.4 million. In comparison, the first quarter of 2010 included other income of \$10.4 million, which primarily related to a receipt in January 2010 of \$8.9 million being the balance of the proceeds related to the establishment of the jointly-owned entity in 2009 with Brookfield Properties Limited ("BPL"), a company related to Brookfield Asset Management Inc. ("BAM").

Financial Position and Liquidity

	Three months ended March 31,	
	2011	2010
<i>(millions of dollars except where noted)</i>		
Cash provided by operating activities	\$ 35.1	\$ 12.3
Cash provided by (used in) investing activities	22.4	(1.2)
Cash used in financing activities	(33.6)	(15.8)
Cash used to construct capitalized logging roads	(1.0)	(1.5)
Cash used to acquire property, plant, and equipment	(1.9)	(0.2)
	March 31	December 31
	2011	2010
Total liquidity ⁽¹⁾	\$ 95.2	\$ 84.6
Net debt ⁽²⁾	45.2	99.8
Financial ratios:		
Current assets to current liabilities	2.45	2.50
Net debt to capitalization ⁽³⁾	0.12	0.23

⁽¹⁾ Total liquidity comprises cash and cash equivalents and available credit under the Company's revolving credit facility and revolving term loan.

⁽²⁾ Net debt is defined as the sum of long-term debt, current portion of long-term debt, revolving credit facility, less cash and cash equivalents.

⁽³⁾ Capitalization comprises net debt and shareholders equity

Cash provided by operating activities in the first quarter of 2011 amounted to \$35.1 million compared to cash provided of \$12.3 million in the same period last year. 2011 cash flows from continuing operations were primarily driven by a \$25.1 million decrease in working capital over the quarter, whereas in the first quarter of

2010 working capital increased by \$7.2 million. In the first quarter of 2011 inventories declined by \$17.2 million primarily due to a reduction in the inventory of logs held at the end of the first quarter compared to December 31, 2010. The reduction in log inventory reflects production being impacted by adverse weather conditions, and also relatively strong log demand in the quarter. Cash generated by operations before the change in non-cash working capital was \$10.0 million in the first quarter of 2011 which is \$9.5 million less than the cash from operations of \$19.5 million in the first quarter of 2010. The operating results for the two periods were relatively consistent, but the 2010 figure includes the net gain of \$8.9 million relating to the reorganization of WFP Forest Products Ltd., referred to earlier.

Cash used for additions to property, plant and equipment and capitalized logging roads in the first quarter of 2011 was \$2.9 million compared to \$1.7 million in the first quarter of 2010. The increase reflects capital spending to build required timberlands infrastructure and is reflective of stronger demand for products.

In the first quarter of 2011, the Company paid down its non-revolving term loan by \$31.2 million as a result of cash generated from the sales of non-core assets in the quarter of \$25.3 million with the balance being paid from the \$5.2 million cash received at the end of 2010 as reimbursement by the Province of British Columbia for costs incurred by Western with respect to the Forestry Revitalization Plan timber take-back areas. In the first quarter of 2010 the revolving credit facility was paid down by \$12.9 million, and by the end of 2010 this facility was not drawn upon.

At March 31, 2011, Western's total liquidity had increased to \$95.2 million from \$84.6 million at the end of 2010 and from the \$54.5 million of liquidity available at March 31, 2010. Liquidity is comprised of cash of \$28.7 million and availability under the secured revolving credit line of \$66.5 million at March 31, 2011. The increase in the liquidity availability compared to March 31, 2010 is largely a function of the improved availability under the amended financing agreements and the fact that improved cash generated from operations required less to be drawn down on the revolving credit facility.

Any net proceeds realized from the future sale of non-core assets will be used to repay the term loan. Based on its financial position at March 31, 2011 and its current forecasts the Company expects to operate as a going concern for the foreseeable future.

Changes in Accounting Policies

Effective January 1, 2011, Canadian publically listed entities were required to prepare their financial statements in accordance with IFRS. Due to the requirement to present comparative financial information, the effective transition date for the Company is January 1, 2010. The three months ended March 31, 2011 is our first reporting period under IFRS. Full disclosure of the Company's accounting policies in accordance with IFRS can be found in Note 2 to the interim financial statements. The interim financial statements also include reconciliations of the previously disclosed comparative periods financial statements prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") to IFRS as set out in Note 4.

New Standards and Interpretations

The following new Standard is not yet effective for the year ended December 31, 2011, and has not been applied in preparing these unaudited condensed consolidated interim financial statements:

Financial instruments

IFRS 9 Financial instruments ("IFRS 9") was issued by the IASB on November 12, 2009 and will replace IAS 39 *Financial Instruments: Recognition and Measurement* ("IAS 39"). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. The Company has not yet determined the impact of IFRS 9 on its financial statements.

Evaluation of Disclosure Controls and Procedures

As required by National Instrument 52-109 issued by the Canadian Securities Administrators, Western carried out an evaluation of the design and effectiveness of the Company's disclosure controls and procedures and internal controls over financial reporting as of December 31, 2010. The evaluation was carried out under the

supervision and with the participation of the Chief Executive Officer (“CEO”) and the Chief Financial Officer (“CFO”). Based on the evaluation, Western’s CEO and CFO concluded that the Company’s disclosure controls and procedures are effective in providing reasonable assurance that material information relating to Western and its consolidated subsidiaries is made known to them by others within those entities, particularly during the period in which the interim filings are being prepared. In addition, Western’s CEO and CFO concluded that the Company’s internal controls over financial reporting are effective in providing reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for Western and its consolidated subsidiaries for the period in which the interim filings are being prepared.

There were no changes in the controls which materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting during the first quarter of 2011.

Risks and Uncertainties

The business of the Company is subject to a number of risks and uncertainties, including those described in the 2010 Annual Report which can be found on SEDAR, at <http://www.sedar.com>. Any of the risks and uncertainties described in the above-noted document could have a material adverse affect on our operations and financial condition and cash flows and, accordingly, should be carefully considered in evaluating Western’s business.

Outlook and Strategy

As expected, the pace of worldwide economic recovery continues to be slow into 2011. Although most signs point to the fact that economic conditions have improved, it would appear that full recovery still will not occur for several years. Despite weak underlying demand in North America, lumber prices remain reasonably strong reflecting growing shipments of hemlock and douglas fir products in our key markets of Japan and China

Demand for forest products continues to rise in China. The migration of Chinese citizens to cities is driving an affordable housing construction boom there. It is now estimated that twenty million new residences are required each year to keep pace with this trend. At the same time, the growth of the middle class in China is fuelling demand for higher end wood frame construction. With the market weakness in the US, our commodity program continues to focus on China. We expect the Chinese market to be our highest volume lumber market for 2011.

The earthquake and resulting devastation in Japan has created some uncertainty in that market. The focus of the government is initially on clean up, which will then shift towards rebuilding. It is estimated that approximately 150,000 buildings were destroyed in the earthquake and resulting tsunami. The infrastructure damage is expected to slow lumber demand in the immediate term; however in the longer term demand for our products is expected to increase. Western intends to participate in certain government/industry relief projects that will aid in the rebuilding of Japan.

The US housing market continues to have deep structural issues which will undermine the housing market recovery there. As recently announced US housing data suggests, significant recovery will be delayed due to high unemployment rates, limited access to credit and high foreclosure rates. Another factor reducing margins to US denominated markets is the strengthening of the Canadian dollar. The Canadian dollar has appreciated against the US dollar by 5% over the same period last year. Currently the only US markets for our products that are showing some promise are certain cedar and niche markets, such as door and window products.

Cedar demand in the US has improved as distributors increase their inventories prior to the spring buying season. In addition, competitors in this market segment have recently taken downtime, in response to the strengthening Canadian dollar. The niche business in North America remains strong, with orders being robust through the second quarter of 2011. We will continue to diversify our customer and product base in this market segment.

The Company continues to monitor the request for arbitration made by the US under the Canada/US Softwood Lumber Trade Agreement. A ruling from the London Court of International Arbitration is expected to take up to a year to be released and it is not possible to predict the outcome of their claims, or whether they would potentially have any impact on Western since they are directed specifically at British Columbia interior practices.

Our previously announced plans to embark on a \$125 million strategic capital program are currently underway. The capital options continue to be evaluated and it is expected that we will spend \$10 million on strategic, high return projects over the latter half of 2011. We also plan to spend an additional \$20 million of capital related to maintenance over this period. However such projects will continue to be thoroughly evaluated in light of the economic uncertainty that currently exists. We also continue to focus on cost reduction and balancing our working capital requirements with market demand in the coming months.

Western will continue to pursue opportunities to sell non-core or other land assets at reasonable values. However, our net debt and liquidity situation has dramatically improved over the past year, so the impetus to make such sales has greatly diminished. Any proceeds will first be first directed to reduce or eliminate long-term debt with any surplus used to provide additional liquidity.

Outstanding Share Data

As of May 9, 2011 there were 128,625,623 Common Shares and 338,945,860 Non-Voting Shares issued and outstanding. Brookfield Special Situations Management Limited (“BSSML”) controls and directs 49% of the Company’s Common Shares and 100% of the Non-Voting Shares. The Company may convert the Non-Voting Shares into Common Shares on a one-for-one basis, in whole or in part, at any time in its sole discretion, provided that the Board of Directors is at that time of the opinion that to do so would not have a material adverse effect on the Company’s business, financial condition or business prospects.

Western has reserved 10,000,000 Common Shares for issuance upon the exercise of options granted under the Company’s incentive stock option plan. On February 23, 2011 a further 1,700,000 options were granted under the plan. As of May 9, 2011, 6,441,795 options were outstanding under the Company’s incentive stock option plan.

Related Parties

By virtue of the BAM voting arrangements with BSSML, BAM is related to the Company. Western has certain arrangements with entities related to BAM to acquire and sell logs, lease certain facilities, provide access to roads and other areas, and acquire other services including insurance and the provision of a foreign exchange facility, all in the normal course and at market rates or at cost. During the first quarter of 2011, the Company paid entities related to BAM \$2.9 million in connection with these arrangements.

On January 4, 2011, the Company exercised its option to sell its equity interest in WFP Forest Products Ltd., the entity that held the jointly-owned entity established in 2009 between the Company and BPL receiving \$2.4 million as consideration for the sale of its interest, and the right of first offer on certain land was extinguished.

Public Securities Filings

Readers may access other information about the Company, including the Annual Information Form and additional disclosure documents, reports, statements and other information that are filed with the Canadian securities regulatory authorities, on SEDAR at www.sedar.com.

On behalf of the Board of Directors

Dominic Gammiero

Chairman

Vancouver, BC,

May 9, 2011

Lee Doney

Vice-Chairman

Management's Discussion and Analysis – Appendix A

Summary of Selected Results for the Last Eight Quarters (Unaudited)

(millions of dollars except per share amounts and where noted)

	Financial results prepared under IFRS					Financial results prepared under Canadian GAAP		
	2011	2010				2009		
	1 st	4 th	3 rd	2 nd	1 st	4 th	3 rd	2 nd
Average Exchange Rate – Cdn \$ to purchase one US \$	0.9858	1.013	1.039	1.029	1.040	1.056	1.098	1.167
Sales								
Lumber	129.0	118.1	123.7	131.1	102.2	96.3	111.8	101.9
Logs	36.3	38.8	39.1	36.6	24.5	32.5	25.5	25.3
By-products	15.5	15.7	12.7	13.8	11.6	10.5	12.6	11.5
Total sales	180.8	172.6	175.5	181.5	138.3	139.3	149.9	138.7
Lumber								
Shipments – millions of board feet	183	168	165	189	147	140	157	145
Price – per thousand board feet	705	703	750	694	695	688	712	703
Logs								
Shipments – thousands of cubic meters	504	646	642	640	414	528	413	406
Price – per cubic metre*	68	60	61	57	59	62	62	62
Selling and administration	6.6	7.6	5.9	5.7	5.4	5.6	5.8	5.9
EBITDA	8.2	5.8	11.6	21.9	9.3	2.3	(5.2)	(16.0)
Depreciation and amortization	(5.6)	(5.2)	(5.4)	(6.9)	(5.9)	(7.2)	(7.3)	(8.2)
Changes in fair value of biological assets	(0.6)	(2.7)	0.7	(0.6)	(0.7)	-	-	-
Reversal of impairment	-	18.5	-	-	-	-	-	-
Operating restructuring items	(0.3)	(0.1)	(0.6)	(0.9)	-	0.3	(2.3)	(3.5)
Finance costs	(1.9)	(2.8)	(3.5)	(3.4)	(3.2)	(3.2)	(2.9)	(2.3)
Other income (expenses)	(0.5)	6.3	(0.3)	0.3	10.4	5.1	1.7	0.5
Income taxes	-	0.6	(0.1)	(0.3)	(0.2)	-	(0.1)	-
Net income (loss) from continuing operations	(0.7)	20.4	2.4	10.1	9.7	(2.7)	(16.1)	(29.5)
Net loss from discontinued operations	(0.3)	(0.3)	(0.3)	(0.3)	(0.6)	(0.4)	(0.5)	(0.6)
Net income (loss)	(1.0)	20.1	2.1	9.8	9.1	(3.1)	(16.6)	(30.1)
EBITDA as % of sales	4.5%	3.4%	6.6%	12.1%	6.7%	1.7%	(3.5)%	(11.5)%
Earnings per share:								
Net income (loss) basic and diluted	-	0.04	0.00	0.02	0.02	(0.01)	(0.04)	(0.06)
Net income (loss) from continuing operations basic and diluted	-	0.04	0.01	0.02	0.02	(0.01)	(0.04)	(0.06)

* Note - the log revenue used to determine average price per cubic metre in Q1 of 2011 was adjusted to reflect revenues recognized of \$2.0 million associated with shipping costs arranged in the period to enable comparability of unit prices.

The presentation of the most current five quarters above as required under IFRS reporting rules has not materially impacted the comparability of these quarters with the previous three quarters that were prepared under Canadian GAAP rules, other than the reversal of the impairment of \$18.5 million as indicated in the fourth quarter of 2010.

In a normal operating year there is some seasonality to the Company's operations with higher lumber sales in the second and third quarters when construction activity, particularly in key markets such as the US, has historically tended to be higher. Logging activity may also vary depending on weather conditions such as rain, snow and ice in the winter and the threat of forest fires in the summer.

The category of "Other income (expense)" comprises gains on the sale of various non-core assets and other receipts which can be unpredictable in their timing. More material transactions of this nature occurred in the first and fourth quarters of 2010, and the fourth quarter of 2009. The downturn in the forest products industry that was experienced most significantly in 2008 and 2009 brought associated production curtailments, which are reflected most significantly in the results of the second, third and fourth quarters of 2009 and the first quarter of 2010. The second and third quarters of 2009 included more significant charges for restructuring.

Western Forest Products Inc.

Unaudited Condensed Consolidated Interim Financial Statements

For the three months ended March 31, 2011 and 2010

Western Forest Products Inc.

Condensed Consolidated Statements of Financial Position

(Expressed in millions of Canadian dollars) (unaudited)

	March 31, 2011	December 31, 2010	January 1, 2010
Assets			
Current assets:			
Cash and cash equivalents	\$ 28.7	\$ 5.1	\$ 8.1
Trade and other receivables	52.3	58.7	39.7
Inventory ^(Note 9)	112.4	129.6	105.2
Prepaid expenses and other assets	5.8	4.8	3.8
	<u>199.2</u>	<u>198.2</u>	<u>156.8</u>
Non-current assets:			
Property, plant and equipment ^(Note 10)	194.6	205.4	230.0
Intangible assets ^(Note 10)	130.2	132.8	117.5
Biological assets ^(Note 11)	61.5	77.7	85.7
Other assets	13.0	13.8	10.9
	<u>\$ 598.5</u>	<u>\$ 627.9</u>	<u>\$ 600.9</u>
Liabilities and Shareholders' Equity			
Current liabilities:			
Revolving credit facility ^(Note 12)	\$ -	\$ -	\$ 15.3
Accounts payable and accrued liabilities	63.1	61.6	44.9
Silviculture provision ^(Note 14)	12.0	11.5	10.3
Current portion of long-term debt ^(Note 13)	-	-	45.2
Discontinued operations	6.2	6.2	6.1
	<u>81.3</u>	<u>79.3</u>	<u>121.8</u>
Non-current liabilities:			
Long-term debt ^(Note 13)	73.9	104.9	74.5
Silviculture provision ^(Note 14)	16.3	15.8	15.7
Other liabilities ^(Note 15)	21.5	23.3	15.6
Deferred revenue	69.9	70.4	72.4
	<u>262.9</u>	<u>293.7</u>	<u>300.0</u>
Shareholders' equity:			
Share capital - voting shares ^(Note 17)	412.3	412.3	412.3
Share capital - non-voting shares ^(Note 17)	187.5	187.5	187.5
Contributed surplus	3.1	3.0	2.7
Accumulated other comprehensive income	23.9	23.9	23.9
Deficit	(291.2)	(292.5)	(325.5)
	<u>335.6</u>	<u>334.2</u>	<u>300.9</u>
	<u>\$ 598.5</u>	<u>\$ 627.9</u>	<u>\$ 600.9</u>

Commitments and Contingencies ^(Note 18)

See accompanying notes to these unaudited condensed consolidated interim financial statements

Approved on behalf of the Board:

"Dominic Gammiero"
Chairman

"Lee Doney"
Vice Chairman

Western Forest Products Inc.

Condensed Consolidated Statements of Comprehensive Income

(Expressed in millions of Canadian dollars except for share and per share amounts) (unaudited)

	Three months ended March 31	
	2011	2010
Revenue	\$ 180.8	\$ 138.3
Cost and expenses:		
Cost of goods sold	149.7	115.6
Export tax	1.4	1.0
Freight	21.1	13.6
Selling and administration	6.6	5.4
	<u>178.8</u>	<u>135.6</u>
	<u>2.0</u>	<u>2.7</u>
Operating restructuring items ^(Note 20)	(0.3)	-
Other income (expenses) ^(Note 21)	(0.5)	10.4
Operating income	<u>1.2</u>	<u>13.1</u>
Finance costs	(1.9)	(3.2)
Income (loss) before income taxes	(0.7)	9.9
Income tax expense	-	(0.2)
Net income (loss) from continuing operations	(0.7)	9.7
Net loss from discontinued operations ^(Note 7)	(0.3)	(0.6)
Net income (loss) for the period	<u>(1.0)</u>	<u>9.1</u>
Other comprehensive income (loss)		
Defined benefit plan actuarial gains (losses), net of tax	2.3	(7.4)
Total comprehensive income for the period	<u>\$ 1.3</u>	<u>\$ 1.7</u>
Net income (loss) per share (in dollars):		
Basic and diluted earnings per share	-	0.02
Basic and diluted earnings per share - continuing operations	<u>-</u>	<u>0.02</u>
Weighted average number of shares outstanding (thousands)		
Basic	467,571	467,571
Diluted	472,899	473,558

See accompanying notes to these unaudited condensed consolidated interim financial statements

Western Forest Products Inc.

Condensed Consolidated Statements of Cash Flows

(Expressed in millions of Canadian dollars) (unaudited)

	Three months ended March 31	
	2011	2010
Cash provided by (used in):		
Operating activities:		
Net income (loss) from continuing operations	\$ (0.7)	\$ 9.7
Items not involving cash:		
Amortization of property, plant and equipment	4.7	5.1
Amortization of intangible assets	0.9	0.8
(Gain) loss on disposal of assets	0.8	(0.2)
Changes in fair value of biological assets	0.6	0.7
Finance costs	1.9	3.2
Other	1.8	0.2
	<u>10.0</u>	<u>19.5</u>
Changes in non-cash working capital items:		
Trade and other receivables	6.4	(4.9)
Inventory	17.2	(8.4)
Prepaid expenses and other assets	(1.0)	(0.8)
Silviculture provision	1.0	1.0
Accounts payable and accrued liabilities	1.5	5.9
	<u>25.1</u>	<u>(7.2)</u>
	<u>35.1</u>	<u>12.3</u>
Investing activities:		
Additions to property, plant and equipment	(2.9)	(1.7)
Proceeds on disposals of assets	25.3	0.5
	<u>22.4</u>	<u>(1.2)</u>
Financing activities:		
Changes in revolving credit facility	-	(12.9)
Interest paid	(2.3)	(2.4)
Repayment of long-term debt	(31.2)	(0.5)
Refinancing fees	(0.1)	-
	<u>(33.6)</u>	<u>(15.8)</u>
Cash provided by (used in) continuing operations	23.9	(4.7)
Cash used in discontinued operations	(0.3)	(0.5)
Increase (decrease) in cash and cash equivalents	23.6	(5.2)
Cash and cash equivalents, beginning of period	5.1	8.1
Cash and cash equivalents, end of period	<u>\$ 28.7</u>	<u>\$ 2.9</u>

See accompanying notes to these unaudited condensed consolidated interim financial statements

Western Forest Products Inc.

Condensed Consolidated Statements of Changes in Shareholders' Equity

(Expressed in millions of Canadian dollars) (unaudited)

	Share Capital	Contributed Surplus	Revaluation Reserve	Deficit	Total equity
Balance at January 1, 2010	599.8	2.7	23.9	(325.5)	300.9
Net income (loss) for the period	-	-	-	9.1	9.1
Other comprehensive income (loss):					
Defined benefit plan actuarial gains (losses) recognized, net of tax	-	-	-	(7.4)	(7.4)
Total comprehensive income for the period	-	-	-	1.7	1.7
Share-based payment transactions recognized in equity	-	0.1	-	-	0.1
Total transactions with owners, recorded directly in equity	-	0.1	-	-	0.1
Balance at March 31, 2010	599.8	2.8	23.9	(323.8)	302.7
Balance at January 1, 2011	599.8	3.0	23.9	(292.5)	334.2
Net income (loss) for the period	-	-	-	(1.0)	(1.0)
Other comprehensive income (loss):					
Defined benefit plan actuarial gains (losses) recognized, net of tax	-	-	-	2.3	2.3
Total comprehensive income (loss) for the period	-	-	-	1.3	1.3
Share-based payment transactions recognized in equity	-	0.1	-	-	0.1
Total transactions with owners, recorded directly in equity	-	0.1	-	-	0.1
Balance at March 31, 2011	599.8	3.1	23.9	(291.2)	335.6

See accompanying notes to these unaudited condensed consolidated interim financial statements

Western Forest Products Inc.

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Notes to the Unaudited Condensed Consolidated Interim Financial Statements

(Tabular amounts expressed in millions of Canadian dollars)

1. General Information

Western Forest Products Inc. ("Western" or the "Company") is a major integrated softwood forest products company domiciled in Canada, operating in the coastal region of British Columbia. The unaudited condensed consolidated interim financial statements of the Company as at March 31, 2011 and for the three months ended March 31, 2011 and 2010 comprises the Company and its subsidiaries. The Company's primary business includes timber harvesting, reforestation, forest management, sawmilling logs into lumber, wood chips, and value-added lumber remanufacturing. Western's lumber products are currently sold in over 30 countries worldwide.

The consolidated financial statements of the Company as at and for the year ended December 31, 2010 which were prepared under Canadian Generally Accepted Accounting Principles ("Canadian GAAP") are available on www.sedar.com.

These unaudited condensed consolidated interim financial statements ("interim financial statements") were approved by the Board of Directors on May 9, 2011.

2. Summary of Significant Accounting Policies

(a) Statement of compliance and basis of presentation

Effective January 1, 2011, the Company fully adopted International Financial Reporting Standards ('IFRS') as the basis for preparation of financial information and accounting.

The interim financial statements are for the three months ended March 31, 2011. Because they are part of the first fiscal year accounted for under IFRS, they have been prepared in accordance with IAS 34, *Interim Financial Reporting*, and are covered by IFRS 1, *First-time Adoption of IFRS*. As a result, these interim financial statements may provide additional disclosure not normally expected in interim financial statements. These interim financial statements do not include all of the information required for full annual financial statements.

Reconciliations and descriptions of the effect of the transition to IFRS on the Company's financial position, financial performance and cash flows are provided in Note 4 – Transition to IFRS. This note includes reconciliations of equity and total comprehensive income for comparative periods and of equity at the date of transition reported under Canadian GAAP, to those reported for those periods and at the date of transition under IFRS.

These interim financial statements have been prepared on a going concern basis. The going concern basis of presentation assumes the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. Based on its financial position at March 31, 2011 and its current forecasts, the Company expects it will be able to continue to operate as a going concern for the foreseeable future.

The preparation of interim financial statements in accordance with IAS 34 requires the use of certain critical accounting estimates. It also requires Management to exercise judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or where assumptions and estimates are significant to the interim financial statements, are disclosed in Note 3 – Critical Accounting Estimates and Judgements. Actual results may differ from these estimates.

The accounting policies set out below have been applied consistently to all periods presented in the interim financial statements and in preparing the opening IFRS statement of financial position at January 1, 2010 for the purposes of transition to IFRS.

(b) Basis of measurement

The interim financial statements have been prepared on the historical cost basis except for the following material items in the statement of financial position:

- Biological assets are measured at fair value less costs to sell;
- Land within property, plant and equipment is measured at fair value;

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(Tabular amounts expressed in millions of Canadian dollars)

- Liabilities for cash-settled share-based payment transactions are measured at fair value at each reporting period and liabilities for equity-settled share based payment transactions are measured at fair value at grant date;
- Derivative financial instruments are measured at fair value; and
- The defined benefit liability is recognized as the net total of the plan assets, plus unrecognized past service cost, less the present value of the defined benefit obligation.

(c) Consolidation

As part of its transition to IFRS, the Company elected not to restate business combinations that occurred prior to January 1, 2010.

Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are de-consolidated from the date on which control ceases.

The principal wholly-owned operating subsidiaries of the Company at March 31, 2011 are Western Lumber Sales Limited (which sells into the United States), MacMillan Bloedel KK (which sells into Japan), and WFP Quatsino Navigation Limited (the beneficial owner of a number of the Company's non-core assets).

Inter-company transactions, balances and unrealized gains on inter-company transactions are eliminated in preparing these interim financial statements. Unrealized losses are also eliminated in the same way unless the transaction provides evidence of an impairment of the asset transferred.

(d) Operating segments

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. The Company is an integrated Canadian forest products company operating in one business segment comprised of timber harvesting, log sales and lumber manufacturing and sales in world-wide markets.

A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments. Western's log and lumber products are currently sold in over 30 countries worldwide, with sales to customers in Canada, the United States, Asia and Europe representing over 95% of the Company's sales. Substantially all of Western's property, plant and equipment, biological assets and intangible assets are located in British Columbia, Canada.

(e) Foreign currency translation

(i) Functional and presentation currency

These interim financial statements are presented in the Canadian dollar which is the Company's and its subsidiaries functional currency. Management believes that the Canadian dollar best reflects the currency of the primary economic environment in which Western operates.

(ii) Transactions and balances

Foreign currency transactions are translated into Canadian dollars using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at balance sheet date exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in net income (loss) for the period. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated into Canadian dollars at foreign exchange rates at the date the fair value was determined.

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(Tabular amounts expressed in millions of Canadian dollars)

(f) Property, plant and equipment

All items of property, plant and equipment are measured at cost, less accumulated depreciation and accumulated impairment losses, except for land, which is measured at fair value at each balance sheet date.

Cost includes expenditures that are directly attributable to the acquisition of the asset. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment. The cost of replacing a component of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Company, and its cost can be measured reliably. The carrying amount of the replaced component is derecognized. All other repairs and maintenance are recognized in net income (loss) for the period as incurred.

Fair value increases in the carrying amount of land are credited to other comprehensive income and included within the revaluation reserve in shareholders' equity. Decreases that offset previous increases of the same item of land are recognized in other comprehensive income. All other decreases are recognized immediately in net income (loss) for the period.

Depreciation is based on the depreciable amount of an item of property, plant and equipment, which is the cost of an item, less its residual value. Depreciation is calculated using the straight-line method and is recognized in net income (loss) over the estimated useful life of each component of an item of property, plant and equipment. Land is not depreciated. The estimated useful lives for the current and comparable periods are as follows:

- Buildings and equipment 5 – 20 years
- Logging roads 9 – 20 years

Residual values, depreciation methods and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Gains and losses on disposals are determined by comparing proceeds from disposal with the carrying amount of the item of property, plant and equipment and are recognized in net income (loss) for the period in which the disposal occurs.

(g) Biological assets

Standing timber on privately held forest land that is managed for timber production is characterized as a biological asset. Accordingly, on each balance sheet date, the biological asset is valued at its fair value less costs to sell with any change therein recognized in net income (loss) for the period. Costs to sell include all costs that would be necessary to sell the assets. Standing timber is transferred to inventory at its fair value less costs to sell at the date the logs are removed from the forest. Land under standing timber is measured at fair value at each balance sheet date and included in property, plant and equipment.

(h) Intangible assets

Crown timber tenures are the contractual arrangements between the Company and the Provincial Government whereby the Company gains the right to harvest timber. All of the Company's timber licenses are accounted for as acquired finite lived intangible assets. Accordingly these are valued at their acquired cost less accumulated amortization and any accumulated impairment losses. Amortization is recognized on a straight-line basis over 40 years, the estimated useful life of these crown timber tenures. Amortization methods, useful lives and residual values are reviewed, and adjusted if appropriate, at each balance sheet date.

(i) Impairment of non-financial assets

Assets that are subject to amortization are tested for impairment whenever events or changes in circumstance indicate that the carrying amount may not be recoverable. An impairment loss is recognized in net income (loss) for the period for the amount by which the asset's carrying amount

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exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped into cash generating units ("CGU") which are the lowest levels for which there are separately identifiable cash flows.

Impairment losses recognized in prior periods are assessed at each balance sheet date for any indication that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the assets' adjusted carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognized.

(j) Inventories

Inventory, other than supplies which are valued at specific cost, are valued at the lower of cost and net realizable value ("NRV") as described below.

- (i)* Lumber by species and facility (hemlock and balsam, douglas fir and cedar);
- (ii)* Logs by end use sort (saw logs and pulp logs).

The cost of inventories includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

The costs of lumber produced carry an average cost of production based on the species and facility where they were produced, determined by actual lumber production costs divided by production volumes.

The costs for logs produced are allocated to logs based on the estimated fair value of the logs produced, except for pulp logs that are carried at market due to the significant difference between the market value of pulp logs compared to production costs.

NRV is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The NRV for logs designated for lumber production is determined on the basis of the logs being converted to lumber with the NRV for the remaining logs based on market log prices.

The cost of standing timber transferred from biological assets is its fair value less costs to sell at the date of harvest.

(k) Cash and cash equivalents

Cash and cash equivalents include cash in bank accounts and highly liquid money market instruments with maturities of 90 days or less from the date of acquisition, and are carried at fair value.

(l) Share capital

The Company's authorized capital consists of an unlimited number of common shares ("the Common Shares"), an unlimited number of non-voting shares ("the Non-Voting Shares") and an unlimited number of preferred shares. Common, Non-Voting and preferred shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction from the proceeds, net of any tax effects.

(m) Long-term debt

Long-term debt is recognized initially at fair value, net of transaction costs incurred. Long-term debt is subsequently carried at amortized cost; any difference between the proceeds and the redemption value is recognized in net income (loss) for the period over the term of the long-term debt using the effective interest method.

(n) Employee benefits

- (i)* Employee post-retirement benefits

The Company has various defined benefit and defined contribution plans that provide pension or other retirement benefits to most of its salaried employees and certain hourly employees not covered by forest industry union plans. The Company also provides other post retirement benefits

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and pension bridging benefits to eligible retired employees. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. A defined contribution plan is a retirement plan under which the Company pays fixed contributions into a separate entity.

The Company's net obligation in respect of its defined benefit plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. Any unrecognized past service costs and the fair value of the plan assets are deducted. The calculation is performed annually by a qualified actuary using the projected benefit actuarial method.

When the calculation results in a benefit to the Company, the recognized asset is limited to the total of any unrecognized past service costs and the present value of economic benefits available in the form of any future refunds from the defined benefit plan or reductions in future contributions to the defined benefit plan. In order to calculate the present value of economic benefits, consideration is given to any minimum funding requirements that apply to any defined benefit plan.

Past-service costs are recognized immediately in net income (loss) for the period, unless the changes to the plans are conditional on the employees remaining in service for a specified period of time ("the vesting period"). In this case, the past-service costs are amortized on a straight-line basis over the vesting period.

The Company recognizes all actuarial gains and losses arising from defined benefit plans immediately in other comprehensive income, and reports them in retained earnings.

For hourly employees covered by forest industry union defined benefit pension plans, the net income (loss) for the period is charged with the Company's contribution as required under the collective agreements.

For its defined contribution plan, the Company makes contributions (currently 7% of employee earnings) to privately administered investment funds on behalf of the Plan members. The Company has no further payment obligations once the contributions have been paid. The contributions are recognized as employee benefit expense in net income (loss) for the period during which services are rendered by employees. Prepaid contributions are recognized as an asset to the extent that a cash refund or a reduction in the future payments is available.

(ii) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Company recognizes termination benefits in net income (loss) for the period when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy. If the benefits are payable more than 12 months after the balance sheet date then they are discounted to their present value.

(iii) Short-term employee benefits

Short-term employee benefit obligations, including bonus plans, are measured on an undiscounted basis and are expensed as the related service is provided.

(iv) Share-based payment transactions

The Company has established share-based payment plans for eligible directors, officers and employees and accounts for these plans using the fair value method. The grant-date fair value of share-based payment awards (i.e. options) is recognized as an employee expense, with a corresponding increase in equity, over the period that the individual becomes unconditionally entitled to the awards. The fair value of the options is determined using either the Black-Scholes or the Hull-White option pricing models which take into account, as of the grant date, the exercise price, the expected life of the options, the current price of the underlying stock and its expected volatility, expected dividends on the shares, and the risk-free interest rate over the expected life of the option. In the case of options issued in 2010 and 2009, the options are only exercisable when

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the share price exceeds a barrier price of \$0.70 for 60 consecutive days on a volume weighted average price basis. With this additional requirement for the share price to exceed a minimum level before the options become exercisable, it is necessary to utilize the Hull-White model as the Black-Scholes model used for valuing earlier granted options is no longer applicable. All options which were previously granted and do not contain the minimum price requirement continue to be valued using the Black-Scholes model. Inherent in all option pricing models is the use of highly subjective estimates, including expected volatility of the underlying shares. The Company bases its estimates of volatility on historical share prices of the Company itself as well as those of comparable companies with longer trading histories. Cash consideration received from employees when they exercise the options is credited to share capital, as is the previously calculated fair value included in contributed surplus.

The grant-date fair value of the amount payable to eligible directors, officers and employees in respect of deferred share units ("DSUs"), which are cash-settled, is recognized as an employee expense with a corresponding increase in liabilities, over the period that the individuals become unconditionally entitled to payment. The liabilities are re-measured at fair value at each balance sheet date and at settlement date. Any changes in the fair value of the liabilities are recognized in employee expenses in net income (loss) for the period.

(o) Silviculture provision

The Company's provision for silviculture relates to the obligation for reforestation on Crown land and arises as timber is harvested. Reforestation on private timberlands is expensed as incurred. The Company recognizes a provision for silviculture at fair value in the period in which the legal obligation is incurred, with the fair value of the liability at balance sheet date determined with reference to the present value of estimated future cash flows. The pre-tax discount rate used to determine the present value reflects current market assessments of the time value of money and the risks specific to the liability. In periods subsequent to the initial measurement, changes in the liability resulting from revisions to estimated future cost are recognized in cost of sales within net income (loss) for the period as they occur. The unwinding of the discount associated with the provision to reflect the passage of time is included in finance costs within net income (loss) for the period.

(p) Revenue recognition

Revenue from the sale of goods is measured at the fair value of the consideration received or receivable, net of rebates and discounts, and after eliminating intercompany sales. Revenue is recognized as soon as the substantial risks and rewards of ownership transfer from the Company to the customer. The timing of the transfers of risks and rewards varies depending on the individual terms of the contract of sale. Lumber and by-product sales are recorded at the time product is shipped and the collection of the amounts is reasonably assured. Consistent with industry practice, log sales are recorded when the customer's order is firm, the logs have been delivered to the transfer location and the collectability of the amount is reasonably assured.

Amounts charged to customers for shipping and handling are recognized as revenue and shipping and handling costs, lumber duties, and export taxes incurred by the Company are recorded in costs and expenses.

(q) Deferred revenue

Deferred revenue is the result of the contractual obligations incurred upon the acquisition of the Englewood Logging Operation and calls for Western to deliver a specified volume of fibre (chips and pulp logs) over the term of the contract. Accordingly, the deferred revenue is amortized into net income (loss) for the period on a straight-line basis over 40 years, being the term of the related fibre supply contract.

(r) Leases

Leases where the lessor retains substantially all the risks and rewards of ownership are classified as operating leases and payments made under operating leases are recognized in net income (loss) for the period on a straight line basis over the period of the lease.

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(s) Finance costs

Finance costs comprise interest expense on long-term debt and the revolving credit facility, unwinding of the discount on the silviculture provision and changes in the fair value of investments recognized immediately through net income (loss). All finance costs are recognized in net income (loss) during the period using the effective interest method.

(t) Financial Instruments

(i) Non-derivative financial assets

The Company classifies its financial assets in the following categories: at fair value through profit and loss, loans and receivables, and held-to-maturity. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

The Company initially recognizes loans and receivables on the date that they are originated. All other financial assets are recognized initially on the trade date at which the Company becomes a party to the contractual provisions of the instrument.

Certain of the Company's investments are classified at fair value through profit and loss. These financial assets are measured at fair value at the balance sheet date with changes therein recognized in net income (loss) for the period.

Loans and receivables comprise trade and other receivables. Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

Held-to-maturity financial assets include certain investments held by the Company. Held-to-maturity financial assets are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition held-to-maturity financial assets are measured at amortized cost using the effective interest method, less any impairment losses.

Cash and cash equivalents comprise cash balances and short-term investments with original maturities of 90 days or less.

A financial asset not carried at fair value through profit or loss is assessed at each balance sheet date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

The Company considers evidence of impairment for receivables and held-to-maturity investment securities at both a specific asset and collective level. In assessing for impairment, the Company uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for Management's judgement for current economic and credit conditions.

An impairment loss is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in net income (loss) for the period and reflected in an allowance against receivables.

(ii) Non-derivative financial liabilities

The Company initially recognizes debt issued on the date that it is originated. The Company's non-derivative financial liabilities consist of long-term debt, the revolving credit facility as well as accounts payable and accrued liabilities. These financial liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

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(iii) Derivative financial instruments

The Company may enter into derivative financial instruments (foreign currency forward contracts) in order to mitigate its exposure to foreign exchange risk. The Company's policy is not to use derivative financial instruments for trading or speculative purposes. These instruments have not been designated as hedges for accounting purposes, and they are carried on the balance sheet at fair value with changes in the (realized and unrealized) fair value being recognized as gains or losses within sales in net income (loss) for the period.

(u) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognized in net income (loss) for the period except to the extent that it relates to items recognized either in other comprehensive income or directly in equity, in which case it is recognized in other comprehensive income or equity respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Deferred tax is recognized using the asset and liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the interim financial statements. Deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects either accounting or taxable profit or loss.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled. Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. Such assets are reviewed at each balance sheet date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(v) Earnings per share

The Company presents basic and diluted earnings per share ("EPS") data for its common shares. Basic EPS is calculated by dividing the net income (loss) attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted EPS is determined by adjusting the net income (loss) attributable to the common shareholders and the weighted average number of common shares outstanding, for the effects of all dilutive potential common shares, which comprise share options granted to employees.

(w) New Standards and interpretations

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended December 31, 2011, and have not been applied in preparing these interim financial statements:

IFRS 9 *Financial instruments* ("IFRS 9") was issued in November 2009 and will replace IAS 39 *Financial Instruments: Recognition and Measurement* ("IAS 39"). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. The Company has not yet determined the impact of IFRS 9 on its financial statements.

3. Critical Accounting Estimates and Judgements

The Company makes estimates and assumptions concerning its future operations. The resulting accounting estimates will seldom equal the related actual results. Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. In preparing these interim financial statements, the significant judgments made by management applying the Company's accounting

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policies and the key sources of estimation uncertainty are expected to be the same as those to be applied in the first annual IFRS financial statements.

The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within 2011 are included within the following notes:

Note 10 – Property, plant and equipment – measurement of the fair value of land

Note 10 – Property, plant and equipment – key assumptions used in discounted cash flows

Note 10 – Intangible assets – key assumptions used in discounted cash flows

Note 11 – Biological assets – measurement of fair value less costs to sell of standing timber

Note 16 – Employee post-retirement benefits – measurement of defined benefit obligations

Note 17 – Share capital – measurement of share-based payment transactions

Note 19 – Financial Instruments – measurement of foreign exchange forward contract derivatives

4. Transition to IFRS

Western's financial statements for the year ended December 31, 2011 will be the first annual financial statements that will be prepared in accordance with IFRS. The accounting policies as described in Note 2 have been applied in preparing the interim financial statements for the three months ended March 31, 2011, as well as for the comparative three months ended March 31, 2010, for the comparative year ended December 31, 2010 and in the preparation of the opening IFRS balance sheet as at January 1, 2010 (the Company's date of transition).

(a) Application of IFRS 1

In preparing these interim financial statements in accordance with IFRS 1, the Company has applied the mandatory exceptions and certain of the optional exemptions from full retrospective application of IFRS.

Western has elected to apply the following optional exemptions in accordance with IFRS 1:

(i) Business combinations exemption

Western has applied the business combinations exemption in IFRS 1. It has not restated business combinations that took place prior to the January 1, 2010 transition date.

(ii) Fair value as deemed cost exemption

Western has elected to measure certain items of property, plant and equipment, primarily roads and bridges, at fair value as at January 1, 2010.

(iii) Employee benefits exemption

Western has elected to recognize all cumulative unrecognized actuarial gains and losses that existed as at January 1, 2010 in retained earnings for all its employee benefit plans.

(iv) Share-based payment transactions

Western has elected not to re-measure equity awards granted after November 7, 2002 that vested prior to the date of transition and liabilities for cash-settled awards that were settled prior to the date of transition.

(v) Arrangements containing a lease

Western has elected not to re-assess arrangements existing at the date of transition, based on the facts and circumstances at that date, in accordance with IFRIC 4.

The remaining IFRS 1 voluntary exemptions either have not or do not apply to the Company at the date of transition to IFRS on January 1, 2010.

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Western has applied the following mandatory exceptions from retrospective application.

(i) Estimates exception

Estimates under IFRS at January 1, 2010 are consistent with estimates made for the same date under Canadian GAAP.

(ii) Assets held for sale and discontinued operations exception

Management has applied IFRS 5, *Non-Current Assets Held for Sale and Discontinued Operations*, prospectively from January 1, 2010. Any assets held for sale or discontinued operations are recognized in accordance with IFRS 5 only from January 1, 2010. Western did not have any assets that met the held-for-sale criteria during the periods presented. No adjustment at January 1, 2010 was required.

(b) Reconciliations between IFRS and Canadian GAAP

In preparing its opening IFRS statement of financial position, the Company has adjusted amounts reported previously in its financial statements prepared in accordance with Canadian GAAP. An explanation of how the transition from Canadian GAAP to IFRS has affected the Company's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany the tables.

Explanation of transition adjustments

1. Reconciliation of equity:

Note	January 1, 2010			March 31, 2010			December 31, 2010		
	Canadian GAAP	Effect of transition to IFRS	IFRS	Canadian GAAP	Effect of transition to IFRS	IFRS	Canadian GAAP	Effect of transition to IFRS	IFRS
Assets									
Current assets:									
	\$ 8.1	\$ -	\$ 8.1	\$ 2.9	\$ -	\$ 2.9	\$ 5.1	\$ -	\$ 5.1
Cash and cash equivalents									
Trade and other receivables	39.7	-	39.7	44.6	-	44.6	58.7	-	58.7
Inventory	f 105.2	-	105.2	112.3	1.3	113.6	128.9	0.7	129.6
Prepaid expenses and other assets	3.8	-	3.8	4.6	-	4.6	4.8	-	4.8
	<u>156.8</u>	<u>-</u>	<u>156.8</u>	<u>164.4</u>	<u>1.3</u>	<u>165.7</u>	<u>197.5</u>	<u>0.7</u>	<u>198.2</u>
Non-current assets:									
Property, plant and equipment	a,b,c,d,k 405.9	(175.9)	230.0	400.1	(173.8)	226.3	375.8	(170.4)	205.4
Intangible assets	a,g -	117.5	117.5	-	116.7	116.7	-	132.8	132.8
Biological assets	a,e,k -	85.7	85.7	-	85.0	85.0	-	77.7	77.7
Other assets	10.9	-	10.9	10.5	-	10.5	13.8	-	13.8
	<u>\$ 573.6</u>	<u>\$ 27.3</u>	<u>\$ 600.9</u>	<u>\$ 575.0</u>	<u>\$ 29.2</u>	<u>\$ 604.2</u>	<u>\$ 587.1</u>	<u>\$ 40.8</u>	<u>\$ 627.9</u>
Liabilities									
Current liabilities:									
Revolving credit facility	\$ 15.3	\$ -	\$ 15.3	\$ 2.4	\$ -	\$ 2.4	\$ -	\$ -	\$ -
Accounts payable and accrued liabilities	h 55.2	(10.3)	44.9	62.0	(11.2)	50.8	73.0	(11.4)	61.6
Silviculture provision	h -	10.3	10.3	-	11.3	11.3	-	11.5	11.5
Current portion of long-term debt	45.2	-	45.2	120.0	-	120.0	-	-	-
Discontinued operations	6.1	-	6.1	6.3	-	6.3	6.2	-	6.2
	<u>121.8</u>	<u>-</u>	<u>121.8</u>	<u>190.7</u>	<u>0.1</u>	<u>190.8</u>	<u>79.2</u>	<u>0.1</u>	<u>79.3</u>
Non-current liabilities:									
Long-term debt	74.5	-	74.5	-	-	-	104.9	-	104.9
Silviculture provision	h -	15.7	15.7	-	15.7	15.7	-	15.8	15.8
Other liabilities	h,i 29.8	(14.2)	15.6	29.9	(6.8)	23.1	29.5	(6.2)	23.3
Deferred revenue	72.4	-	72.4	71.9	-	71.9	70.4	-	70.4
	<u>298.5</u>	<u>1.5</u>	<u>300.0</u>	<u>292.5</u>	<u>9.0</u>	<u>301.5</u>	<u>284.0</u>	<u>9.7</u>	<u>293.7</u>
Shareholders' equity:									
Share capital	599.8	-	599.8	599.8	-	599.8	599.8	-	599.8
Contributed surplus	j 2.5	0.2	2.7	2.6	0.2	2.8	2.8	0.2	3.0
Accumulated other comprehensive income	b -	23.9	23.9	-	23.9	23.9	-	23.9	23.9
Deficit	(327.2)	1.7	(325.5)	(319.9)	(3.9)	(323.8)	(299.5)	7.0	(292.5)
	<u>275.1</u>	<u>25.8</u>	<u>300.9</u>	<u>282.5</u>	<u>20.2</u>	<u>302.7</u>	<u>303.1</u>	<u>31.1</u>	<u>334.2</u>
	<u>\$ 573.6</u>	<u>\$ 27.3</u>	<u>\$ 600.9</u>	<u>\$ 575.0</u>	<u>\$ 29.2</u>	<u>\$ 604.2</u>	<u>\$ 587.1</u>	<u>\$ 40.8</u>	<u>\$ 627.9</u>

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2. Reconciliation of comprehensive income for the periods:

(Expressed in millions of Canadian dollars) (Unaudited)	Three months ended March 31, 2010			Year ended December 31, 2010			
	Note	Canadian GAAP	Effect of transition to IFRS	IFRS	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue		\$ 138.3	\$ -	\$ 138.3	\$ 667.9	\$ -	\$ 667.9
Cost and expenses:							
Cost of goods sold							
Cost of sales	h,e,f	110.3	(0.6)	109.7	525.6	2.3	527.9
Impairments (recoveries)	g	-	-	-	-	(18.5)	(18.5)
Amortization and depreciation	d,g	7.4	(1.5)	5.9	28.8	(5.4)	23.4
		117.7	(2.1)	115.6	554.4	(21.6)	532.8
Export tax		1.0	-	1.0	3.9	-	3.9
Freight		13.6	-	13.6	66.2	-	66.2
Selling and administration	j	5.4	-	5.4	24.5	0.1	24.6
		137.7	(2.1)	135.6	649.0	(21.5)	627.5
		0.6	2.1	2.7	18.9	21.5	40.4
Operating restructuring items		-	-	-	(1.6)	-	(1.6)
Other income (expenses)	k	10.6	(0.2)	10.4	24.3	(7.6)	16.7
Operating income (loss)		11.2	1.9	13.1	41.6	13.9	55.5
Finance costs	h	(3.1)	(0.1)	(3.2)	(12.4)	(0.5)	(12.9)
Net income before income taxes		8.1	1.8	9.9	29.2	13.4	42.6
Income tax expense		(0.2)	-	(0.2)	-	-	-
Net income from continuing operations		7.9	1.8	9.7	29.2	13.4	42.6
Net loss from discontinued operations		(0.6)	-	(0.6)	(1.5)	-	(1.5)
Net income for the period		7.3	1.8	9.1	27.7	13.4	41.1
Other comprehensive income (loss)							
Defined benefit plan actuarial losses, net of taxes	i	-	(7.4)	(7.4)	-	(8.1)	(8.1)
Total comprehensive income (loss) for the period		\$ 7.3	\$ (5.6)	\$ 1.7	\$ 27.7	\$ 5.3	\$ 33.0

3. Reconciliation of Property, Plant and Equipment

	January 1, 2010
Property, plant and equipment, Canadian GAAP	\$ 405.9
Biological and intangible assets - reclassification	a (184.9)
Land - fair value	b 23.9
Logging roads - deemed cost	c 0.9
Buildings & equipment - deemed cost	c 0.7
Buildings & equipment - impairment	d (16.5)
Property, plant and equipment, IFRS	\$ 230.0

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Material adjustments to the Statements of Cash Flows

None of the Company's IFRS transitional adjustments directly impact the cash and cash equivalents balance and result only in adjustments within the cash flow presentation itself. The adjustments required to the Statement of Cash Flows under IFRS arise due to relatively minor income adjustments, primarily a reduction to depreciation and amortization, which resulted in a corresponding non-cash add-back adjustment. In addition, the impairment recovery of \$18.5 million included in the IFRS reconciliation of comprehensive income for the year ended December 31, 2010 is presented as a separate add-back line to net income (loss) from continuing operations in the Statement of Cash Flows as it has no cash impact. There are no other material differences between the Statement of Cash Flows presented under IFRS and the Statement of Cash Flows presented under Canadian GAAP.

Notes:

- a. Under IFRS, the "Property, plant and equipment" line item was reduced by \$16.2 million as a result of re-classifying the Company's standing timber on its private timberlands, which is considered to be a biological asset under IFRS, to a separate line item, titled "Biological assets" (Note e). In addition, the Canadian GAAP net book value of crown timber tenures of \$168.7 million was re-classified from the "Property, plant and equipment" line item to a separate line item, titled "Intangible assets" (Note g).
- b. "Property, plant and equipment" was also impacted by the Company's policy choice of electing to use the revaluation model to fair value its land assets both at transition date and prospectively at each balance sheet date under IFRS, as compared to a historical cost basis of measurement under Canadian GAAP. As at January 1, 2010, the increase that resulted from this election was \$23.9 million with a corresponding credit to the revaluation reserve, a component of accumulated other comprehensive income and shareholders' equity.
- c. Western adopted the transitional optional exemption of valuing certain items of its "Property, plant and equipment", primarily roads and bridges, at fair value at transition date, which is then considered to be the deemed cost of those assets prospectively. The net impact of this was an increase to the Canadian GAAP net book value of these assets by \$1.6 million.
- d. As a result of applying guidance in IAS 36, the Company's sawmill buildings and equipment, which are categorized within "Property, plant and equipment", recognized an impairment loss on transition date of \$16.5 million. Under Canadian GAAP, the recoverable amount of these assets was calculated on an undiscounted basis. Under IFRSs, the recoverable amount of the CGU was estimated based on its value in use, which requires estimated future cash flows to be discounted. The key assumptions used in this value in use assessment are discussed in Note 10 to the interim financial statements. Depreciation expense associated with sawmill buildings and equipment under IFRS was reduced by \$1.1 million and \$3.8 million when compared to that recognized under Canadian GAAP, for the three months ended March 31, 2010 and for the year ended December 31, 2010, respectively, as a result of the reduced net book value of sawmill buildings and equipment as at January 1 2010.
- e. This adjustment reflects the separation of the Company's standing timber on its private timberlands, which is considered to be a biological asset under IFRS, which was previously included in the line item "Property, plant and equipment" under Canadian GAAP. The net book value of the standing timber reported under Canadian GAAP of \$16.2 million, which was measured at historical cost, was reclassified into "Biological assets", and was subsequently valued at fair value less costs to sell of \$85.7 million on transition to IFRS. The increase of \$69.5 million was credited to "Deficit" in shareholders' equity. The key assumptions used in this valuation are discussed in Note 11 to the interim financial statements. The adjustments to "Biological assets" as at March 31, 2010 and December 31, 2010 reflect this initial adjustment on transition plus the effects of any asset sales and any further adjustments to the fair value less costs to sell including those resulting from timber growth and harvest over the respective periods. These changes to fair value less costs to sell for the Company's biological assets of \$0.7 million for the three months ended March 31, 2010 and \$3.3 million for the year ended December 31, 2010, have been reflected in "cost of sales" in net income (loss) for the period.
- f. As a result of the Company's standing timber on private timberlands being considered a biological asset in accordance with IAS 41, *Agriculture*, the logs harvested from these private timberlands are considered to be agriculture produce that are measured at fair value less costs to sell at the point of harvest, which becomes the deemed cost for the purpose of subsequent accounting under IAS 2,

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Inventories. As a result, an adjustment was required to be made to log and lumber inventory values as reported under Canadian GAAP at March 31 and December 31, 2010 of \$1.3 million and \$0.7 million, respectively, to reflect this guidance under IAS 41 for logs in inventory and harvested from private timberlands.

- g. The adjustment to "Intangible assets" of \$117.5 million reflects the re-classification of the Canadian GAAP net book value for the Company's crown timber tenures from "Property, plant and equipment" of \$168.7 million to "Intangible assets", combined with an impairment charge on transition date as a result of applying IAS 36 *Impairments*, of \$51.2 million. Under Canadian GAAP, the recoverable amount of these assets was calculated on an undiscounted basis. Under IFRSs, the recoverable amount of the CGU was estimated based on its value in use, which requires estimated future cash flows to be discounted. The key assumptions used in this value in use assessment are discussed in Note 10 to the interim financial statements. This impairment charge was partially reversed by \$18.5 million, following an impairment test and reassessment for the CGU as at December 31, 2010 and recognized in cost of goods sold for the year ended December 31, 2010. Amortization expense associated with the crown timber tenures under IFRS was reduced by \$0.4 million and \$1.6 million when compared to that recognized under Canadian GAAP, for the three months ended March 31, 2010 and for the year ended December 31, 2010, respectively, as a result of the reduced net book value of crown timber tenures as at January 1 2010.
- h. Under IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, there are measurement differences when compared to Canadian GAAP. For the Company's silviculture provision, these measurement differences under IFRS relate to the cash flows being discounted using a risk free rate rather than the Company's credit adjusted risk free rate as prescribed under Canadian GAAP. As a result of this measurement difference, the short term and long term components of the silviculture provision were increased by \$0.1 million and \$1.3 million, respectively, with a corresponding charge to the "Deficit" line in shareholders' equity. In addition, the silviculture provision has been separately disclosed on the Statement of Financial Position on transition to IFRS, which resulted in \$10.2 million and \$14.4 million reduction in "Accounts payable and accrued liabilities" and "Other liabilities", respectively, as a result of this re-classification, when compared to Canadian GAAP. On the Statements of Comprehensive Income, the unwind of the discount associated with the silviculture provision under IFRS has been recognized within finance costs rather than within cost of goods sold as under Canadian GAAP.
- i. An adjustment was made to "Other liabilities" to account for the different methodologies under IFRS compared to Canadian GAAP for calculating the liability associated with employee post retirement benefits. Under IFRS, the Company's accounting policy is to recognize all actuarial gains and losses in other comprehensive income. Under Canadian GAAP, the Company's accounting policy was such that the excess of the net accumulated actuarial gain or loss over 10% of the greater of the accrued benefit obligation and the fair value of plan assets was amortized over the remaining service period of the active employees. In addition, the Company has elected that at the date of transition all previously unrecognized cumulative actuarial gains and losses were recognized in retained earnings. This change required an additional liability to be recognized on transition date of \$0.2 million with a corresponding charge to the "Deficit" line in shareholders' equity. Similar re-calculations were made in the three months ended March 31, 2010 and for the year ended December 31, 2010 resulting in additional adjustments to the employee post retirement benefits obligation of \$7.4 million and \$8.1 million, respectively. These adjustments are reflected on the Statements of Comprehensive Income in line item "Other comprehensive income" in the period incurred.
- j. Under Canadian GAAP, Western recognized the fair value of the share-based payment awards, determined at the time of the grant, on a straight-line basis over the five-year vesting period. Under IFRS 2, *Share-Based Payments*, the fair value of each tranche of the award is considered to be a separate grant based on the vesting period, with the fair value of each tranche determined separately and recognized as compensation expense over the term of its respective vesting period. An adjustment was made to "Contributed surplus" to account for the different calculations to be applied under IFRS compared to Canadian GAAP for calculating the cost of share-based payment awards. This change required an increase to "Contributed surplus" to be recognized on transition date of \$0.2 million with a corresponding charge to the "Deficit" line in shareholders' equity.

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- k. The adjustment to "Other income (expenses)" of \$7.6 million relates to the differences between the calculated gains or losses on asset sales under IFRS when compared to Canadian GAAP. These differences result from fair value adjustments to the Canadian GAAP net book values for land, biological assets and certain items of property, plant and equipment as a result of Management's accounting policy elections or requirements under IFRS as outlined under Notes b., c. and e. above.

5. Seasonality of Operations

In a normal operating year, there is some seasonality to the Company's operations with higher lumber sales in the second and third quarters when construction activity in certain key markets has historically tended to be higher. Logging activity may also vary depending on weather conditions such as rain, snow and ice in the winter and the threat of forest fires in the summer.

6. Segmented Information

The Company is an integrated Canadian forest products business operating in one industry segment comprised of timber harvesting and lumber production for marketing and distribution to worldwide markets.

7. Discontinued Operations

In March 2006, the Company closed its Squamish pulp mill located on 213 acres on the mainland coast of British Columbia and exited the pulp business. Subsequent to the closure, the Company sold substantially all of the manufacturing assets of the mill. Ongoing costs including supervision, security and property taxes continue to be expensed as incurred. The real property is one of the Company's portfolio of non-core assets and while site remediation is ongoing, the Company has listed the property for sale.

The following table provides additional information with respect to the discontinued operations:

	Three months ended March 31	
	2011	2010
Net loss from discontinued operations	\$ (0.3)	\$ (0.6)
Cash used in discontinued operations	\$ (0.3)	\$ (0.5)

	March 31, 2011	December 31, 2010	January 1, 2010
Assets of discontinued operations	\$ 2.3	\$ 2.3	\$ 2.2
Liabilities of discontinued operations	\$ 6.2	\$ 6.2	\$ 6.1

8. Related Parties

Brookfield Special Situations Management Limited ("BSSML") controls and directs 49% of the Company's Common Shares and 100% of the Non-Voting Shares. BSSML is a wholly owned subsidiary of Brookfield Asset Management ("BAM").

In addition to the related party transactions identified elsewhere in these interim financial statements, the Company has certain arrangements with entities related to BSSML and BAM to provide financing, acquire and sell logs, lease certain facilities, provide access to roads and other areas, and acquire services including insurance, all in the normal course and at market rates or at cost. The following table summarizes these transactions for the three months ended March 31:

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	Three months ended March 31	
	2011	2010
Costs incurred for:		
Log purchases	\$ 1.8	\$ 1.9
Other	1.1	1.3
	<u>\$ 2.9</u>	<u>\$ 3.2</u>
Income received for:		
Log sales	\$ 0.5	\$ 0.9
Other	2.4	9.4
	<u>\$ 2.9</u>	<u>\$ 10.3</u>

In October 2009, the Company sold certain higher-and-better-use properties in central and northern Vancouver Island (the "HBU Properties") to WFP Forest Products Ltd, ("WFPFPL"), a jointly-owned entity of the Company and Brookfield Properties Limited ("BPL"), a wholly-owned subsidiary of Brookfield Properties Corporation (TSX: BPO.TO), which is in turn related to BAM. The HBU Properties were formerly part of the group of properties that were included in the Company's non-core asset sales program. In connection with the reorganization of WFPFPL as a jointly-owned entity and the sale of those HBU Properties, Western received cash proceeds of \$12.4 million, \$3.0 million in October 2009 and the balance of \$9.4 million on January 4, 2010. As part of the arrangements, WFPFPL had a right of first offer to purchase for possible future development approximately 255 hectares (630 acres) of additional higher-and-better-use properties of the Company in central and northern Vancouver Island. These properties also represent non-core assets of the Company. Western held less than 5% of the equity of WFPFPL and had a right to sell its interest in WFPFPL to BPL for its fair market value at any time on or after January 1, 2011. On January 4, 2011, the Company exercised the option to sell its equity interest in WFPFPL. Western received \$2.4 million as consideration for the sale of its interest, and the right of first offer was extinguished. Brookfield is the manager of WFPFPL, which also holds Carma Developers LP, a limited partnership that carries on a land development business across Western Canada. Because BPL is a related party of BSSML, which is Western's largest shareholder, the transaction constituted a related party transaction.

9. Inventory

The following table summarizes the value of inventory on hand:

	March 31, 2011	December 31, 2010	January 1, 2010
Logs	\$ 58.3	\$ 80.4	\$ 67.3
Lumber	49.0	43.0	32.2
Supplies and other inventories	10.6	10.7	10.2
Provision for write downs	(5.5)	(4.5)	(4.5)
Total value of inventories	<u>\$ 112.4</u>	<u>\$ 129.6</u>	<u>\$ 105.2</u>
Inventory carried at net realisable value	\$ 22.7	\$ 23.7	\$ 19.3

The inventory is pledged as security against the revolving credit line and long-term debt. During the first quarter of 2011, \$149.7 million (2010 - \$115.6 million) of inventory was charged to cost of sales which included an increase in the provision for write-down to net realizable value of \$1.0 million (2010 - \$0.6 million).

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10. Property, Plant, and Equipment and Intangible Assets

	Buildings & equipment	Logging roads	Land	Total property, plant and equipment	Intangible assets
at January 1, 2010					
Cost of capital assets at December 31, 2009	\$ 144.1	\$ 107.6	\$ 108.2	\$ 359.9	\$ 190.4
Accumulated amortization and impairment at December 31, 2009	(71.9)	(67.0)	-	(138.9)	(21.7)
Adjustments on transition to IFRS	(15.8)	0.9	23.9	9.0	(51.2)
Net book value at January 1, 2010	56.4	41.5	132.1	230.0	117.5
at March 31, 2010					
Net book value at January 1, 2010	56.4	41.5	132.1	230.0	117.5
Additions	0.2	1.5	-	1.7	-
Disposals	-	-	(0.3)	(0.3)	-
Depreciation and amortization	(2.3)	(2.8)	-	(5.1)	(0.8)
Net book value at March 31, 2010	\$ 54.3	\$ 40.2	\$ 131.8	\$ 226.3	\$ 116.7
at December 31, 2010					
Cost of capital assets at December 31, 2010	\$ 117.8	\$ 110.7	\$ 119.0	\$ 347.5	\$ 190.4
Accumulated amortization and impairment at December 31, 2010	(69.4)	(72.7)	-	(142.1)	(57.6)
Net book value at December 31, 2010	48.4	38.0	119.0	205.4	132.8
at March 31, 2011					
Net book value at December 31, 2010	48.4	38.0	119.0	205.4	132.8
Additions	1.9	1.0	-	2.9	-
Disposals	(0.2)	(3.7)	(5.1)	(9.0)	(1.7)
Depreciation and amortization	(2.8)	(1.9)	-	(4.7)	(0.9)
Net book value at March 31, 2011	\$ 47.3	\$ 33.4	\$ 113.9	\$ 194.6	\$ 130.2

(a) Intangible assets

Intangible assets are comprised entirely of the Company's crown timber tenures and are considered to be finite lived intangible assets with an estimated useful life of 40 years.

On the transition date, January 1, 2010, as a result of continued losses by the Company and the impact of the global recession on lumber demand and prices in the market, Management determined that indications of possible impairment of the Company's crown timber tenures existed and as a result, the Company conducted an impairment review of its crown timber tenures at January 1, 2010.

Due to the continued concern about the global economic situation and the uncertainties with respect to the US lumber market, the Company conducted a further assessment for impairment at December 31, 2010.

Management considers that the aggregate of all its crown timber tenures constitute a CGU and so tested the recoverable amount of the CGU, which was based on value in use, with the assistance of an independent valuator.

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Value in use was determined by discounting the future cash flows expected to be generated from the continuing use of the CGU. Unless otherwise indicated, value in use at December 31, 2010 was determined similarly as that at January 1, 2010. The calculation of the value in use was based on the following key assumptions:

- Cash flows were projected based on historical and forecasted logging activity levels as estimated by Management while working within the constraints of the annual allowable cut levels imposed by the Chief Forester of British Columbia. Management has assumed a 20 year forecast period given the renewability of the licences and the long term nature of the business;
- Log price assumptions used in the projections were based upon consideration of historical actual log prices and long term trend pricing analysis for the Vancouver log market as published by third party analysts and independent valuers. No inflation was assumed for the first 3 years of the forecast, and a general inflation price increase of 1.7% was assumed for 2013 (December 31, 2010 – 2014) and beyond;
- Cash flows for operating costs associated with the crown timber tenures were assumed to be consistent with past experience, actual operating results and are assumed to grow in line with increases in log pricing;
- A pre-tax discount rate of 11.7% (December 31, 2010 – 11.3%) was used in determining the recoverable amount of the CGU. The discount rate used was estimated based on past experience of a weighted average cost of capital for each of the principal timber tenures of the Company, which was based on possible ranges of debt leveraging of between 15% and 35%, dependent upon the risk assessment attached to each particular timber tenure; and
- A terminal value was determined by assuming a perpetual series of cash flows discounted at the pre-tax discount rate.

As a result of the assessment performed at January 1, 2010, the carrying amount of the CGU was determined to be higher than its recoverable amount and an impairment loss was recognized at the transition date of \$51.2 million directly into retained earnings.

As a result of the value in use assessment performed for the CGU as at December 31, 2010, a reversal of \$18.5 million of the impairment loss previously taken was recognized in cost of goods sold for the year ended December 31, 2010.

(b) Land

As described in Note 2(f) the Company has elected to measure land at fair value at each balance sheet date. At January 1, 2010, Management performed an assessment of the fair value for all of its land holdings using a combination of independent third party valuations, recent comparable land sales, and discounted cash flow analysis as well as considering other publicly available information such as recent market transactions on arm's length terms between willing buyers and sellers, and British Columbia property assessments.

As at January 1, 2010, the increase that resulted from this election was \$23.9 million with a corresponding credit to the revaluation reserve, a component of accumulated other comprehensive income and shareholders' equity.

As a result of the fair value assessment of the land holdings at December 31, 2010, no further fair value adjustments were identified, as the carrying value at December 31, 2010 did not differ materially from the estimated fair value.

If land was stated on an historical cost basis, the carrying value would be as follows:

	<u>March 31, 2011</u>	<u>December 31, 2010</u>	<u>March 31, 2010</u>	<u>January 1, 2010</u>
Cost	\$82.0	\$98.3	\$108.2	\$108.2

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(c) Other property plant and equipment including sawmills

For the same reasons listed above in (i) Management considered it necessary to assess its sawmill buildings and equipment for impairment at the transition date and also at December 31, 2010.

Western's sawmills, in aggregate, are considered to be a single CGU for the purposes of assessing the recoverable amount of the CGU. A internal valuation model was utilized to estimate the recoverable amount of the sawmill CGU based on their value in use by determining discounted future cash flows expected to be generated by the sawmills. Unless otherwise indicated, value in use at December 31, 2010 was determined similarly to that at January 1, 2010. The calculation of the value in use was based on the following key assumptions:

- Cash flows were projected for 9 years based on past experience, actual operating results and the 2010 and 2011 business plans;
- Revenue was projected based on past experience, considerations as to the business plans and a statistical analysis of long-term market price trends for benchmark lumber product sold by species. The anticipated revenue growth during the forecast period was determined based on Management estimates and third party industry sources, and range from -4% to 10% per year for each major category of lumber species during the forecast period;
- Log costs were projected based on the assumption that fibre supply would be acquired at market pricing. These were based on past experience, third party industry sources, including historical Vancouver log market pricing, and Management estimates;
- Other costs, including manufacturing, and selling, general and administrative costs were projected to increase at the inflation rate;
- A pre-tax discount rate of 16.5% was applied in the January 1, 2010 determination of the recoverable amount of the sawmill assets (December 31, 2010 – 16.7%). The discount rate was determined based on Management's estimate of the Company's weighted average cost of capital; and
- A terminal value was determined by applying an earnings multiple to the terminal year earnings before interest, taxes, depreciation and amortization.

As a result of the assessment performed at January 1, 2010, the carrying amount of the sawmill CGU was determined to be higher than its recoverable amount and an impairment loss for sawmill buildings and equipment was recognized at the transition date of \$16.5 million directly into retained earnings.

As a result of the value in use assessment performed for the sawmill CGU as at December 31, 2010, no reversal of impairment or further impairment loss was recognized for the year ended December 31, 2010.

11. Biological Assets

	Three months ended March 31	
	2011	2010
Carrying value at beginning of period	\$ 77.7	\$ 85.7
Disposition of standing timber in the period	(15.6)	-
Change in fair value resulting from growth and pricing	0.4	0.8
Harvested timber transferred to inventory during the period	(1.0)	(1.5)
Carrying value at end of period	<u>\$ 61.5</u>	<u>\$ 85.0</u>

Under IAS 41, *Agriculture*, the Company's private timberlands are classified as a growing forest, with the standing timber recorded as a biological asset at fair value less costs to sell at each balance sheet

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date, and the underlying land considered a component of property, plant and equipment, which the Company has elected to record at fair value at each balance sheet date (Note 10).

At March 31, 2011 standing timber comprised of approximately 25,738 hectares (December 31, 2010: 33,780 hectares), which range from newly planted cut-blocks to old-growth forests. During the quarter, the Company harvested and scaled approximately 111,844 m³ of logs from its private timberlands, which had a fair value less costs to sell of \$7.3 million at the date of harvest (March 31, 2010 70,381m³ - \$4.9 million). The fair value of the Company's standing timber is based on the following:

- Recent comparatives of standing timber
- Direct and indirect costs of sustainable forest management.
- Net present value of future cash flows for standing timber.
- For log pricing assumptions see note 10(i).

Accordingly fair value has been determined using the following significant assumptions:

- (i) Harvestable volumes have been determined as the estimated future volume and current standing volume to be harvested over the sustainable life of the privately held timberlands. The harvestable volume of standing timber is based the net planted area, estimated growth rates, estimated yield per hectare and expected sustainable harvest management practices.
- (ii) The costs associated with the land owned by the Company on which standing timber are grown including land taxes and other costs.
- (iii) The continuation of existing practices with regard to silviculture and harvesting.
- (iv) A discount rate of 7.01% and 6.04% has been applied to the estimated future cash flows in arriving at net present value at December 31, 2010 and 2009, respectively. This discount rate has been determined with reference to the Company's market determined discount rate for this asset type based on advice from an independent expert.

The annual valuation of standing timber was carried out during the fourth quarter of 2009 and 2010 using a consistent methodology for establishing fair value less costs to sell.

The financial risks associated with standing timber are mitigated by the geographical diversification of the asset and management strategies including fire management strategies and regular inspection for pest infestation.

The above disposition primarily relates to the sale of properties to TimberWest Forest Corp. as detailed in Note 21.

12. Revolving Credit Facility

The Company's revolving credit facility, as amended on December 14, 2010, provides for a maximum borrowing amount of \$125.0 million, subject to a borrowing base which is primarily based on eligible accounts receivable and inventory balances. The facility bears interest at Canadian prime plus 0.5% (if availability exceeds \$40.0 million) or 0.75% (if availability is less than \$40.0 million) or at the Company's option, at rates for Bankers' Acceptances or LIBOR based loans plus 2.25% or 2.50%, dependent on the same availability criteria. The revolving credit facility matures on December 14, 2015 subject to any future refinancing requirements of its revolving and non-revolving term loans. At March 31, 2011 and December 31, 2010 no amount was drawn on this facility. At March 31, 2011, \$66.5 million of the facility was unused and available to the Company.

13. Long-Term Debt

The Company's term loans which were renegotiated on December 14, 2010, provide \$106.2 million in two secured term loans: a \$75.0 million revolving term loan and \$31.2 million non-revolving term loan. The non-revolving term loan was paid down by \$31.2 million in the first quarter of 2011, largely from the proceeds of non-core asset sales. The revolving term loan matures on June 14, 2013.

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The term loans bear interest at an index rate, determined as the higher of (i) the Canadian prime rate, and (ii) the 30 day Bankers Acceptance rate plus 1.35%, plus the applicable index rate margin, or at the Company's election, the applicable Bankers Acceptance rate, plus the applicable BA rate margin. The applicable index rate margins range from 2.75% to 5.00% and the applicable BA rate margins range from 3.75% to 6.00% and each is determined quarterly, based on a leverage ratio, calculated as the ratio of total debt to the sum of EBITDA for the twelve months ending on the date of determination. The interest rate for the revolving and non-revolving term loans was 6.75% at March 31, 2011 (December 31, 2010 – 6.03% and 6.75%, respectively).

The Company was in compliance with its financial covenants at March 31, 2011.

During 2010, the Company incurred \$1.3 million of transaction costs in relation to the new financing arrangements. These costs are deferred and are being amortized into interest expense over the term of the term loans using the effective interest rate method. Deferred transaction costs associated with the previous facilities were fully expensed during 2010.

	March 31, 2011	December 31, 2010	January 1, 2010
Canadian dollar debt			
Revolving term loan	\$ 75.0	\$ 75.0	\$ 75.0
Non-revolving term loan	-	31.2	47.3
	<u>75.0</u>	<u>106.2</u>	<u>122.3</u>
Less transaction costs	(1.1)	(1.3)	(2.6)
	<u>73.9</u>	<u>104.9</u>	<u>119.7</u>
Less current portion	-	-	45.2
	<u>\$ 73.9</u>	<u>\$ 104.9</u>	<u>\$ 74.5</u>

14. Silviculture Provision

The Company has a responsibility to reforest timber harvested under various timber rights. Changes in the silviculture provision are as follows:

	Three months ended March 31	
	2011	2010
Silviculture provision, beginning of period	\$ 27.3	\$ 26.0
Silviculture provision charged	2.1	2.1
Silviculture work payments	(0.8)	(1.2)
Disposition of intangible assets	(0.4)	-
Unwind of discount	0.1	0.1
Silviculture provision, end of period	<u>28.3</u>	<u>27.0</u>
Less current portion	12.0	11.3
	<u>\$ 16.3</u>	<u>\$ 15.7</u>

15. Other Liabilities

	March 31, 2011	December 31, 2010	January 1, 2010
Employee post retirement benefits obligation ^(Note 16)	\$ 18.0	\$ 21.1	\$ 13.7
Environmental accruals	1.5	1.5	1.5
Other	2.0	0.7	0.4
	<u>\$ 21.5</u>	<u>\$ 23.3</u>	<u>\$ 15.6</u>

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16. Employee Post-Retirement Benefits

Employee post-retirement benefit expense for both the defined benefit salaried pension and non-pension plans recognized in cost of goods sold is as follows:

	Three months ended March 31	
	2011	2010
Current service costs	\$ 0.1	\$ 0.4
Interest costs	1.6	1.7
Expected return on plan assets	(1.6)	(1.6)
Cost of defined benefit plans	0.1	0.5
Cost of defined contribution plans	2.1	1.7
Total cost of employee post retirement benefits	\$ 2.2	\$ 2.2

The amounts recognized in the balance sheet for for the Company's employee post-employment retirement benefit obligations, consisting of both the defined benefit salaried pension and other non-pension benefits is as follows:

	March 31, 2011	December 31, 2010	January 1, 2010
Present value of funded obligations	\$ (120.9)	\$ (123.2)	\$ (112.0)
Fair value of plan assets	102.9	102.1	98.3
Liability recognized in the balance sheet	\$ (18.0)	\$ (21.1)	\$ (13.7)

The liability recognized in the balance sheet at March 31, 2011 was based on the actuarial gains or losses resulting from estimated changes in the discount rate used to value the defined benefit obligations and estimated differences in actual compared to expected returns on plan assets for the quarter. The change in discount rates was an increase of 0.1% from the rate used at December 31, 2010 of 5.36%, and the estimated actual return on assets in the quarter was 9.6% which was based on the index returns for the target asset mix of the related plans.

17. Share Capital

Issued and outstanding Common and Non-Voting Shares are as follows:

	Number of Common Shares	Amount	Number of Non-Voting shares	Amount
Balance at December 31, 2010 and March 31, 2011	128,625,623	\$412.3	338,945,860	\$187.5

Share-based payment transactions

The Company has an incentive stock option plan (the "Option Plan"), which permits the granting of options to eligible participants to purchase up to an aggregate of 10,000,000 Common Shares.

Each option is exercisable, subject to vesting terms of 20% per year and immediately upon a change in control of the Company, into one Common Share, subject to adjustments, at a price of not less than the closing price of the Common Shares on the Toronto Stock Exchange ("TSX") on the day immediately preceding the grant date. Options granted under the Option Plan expire a maximum of ten years from the date of the grant.

During the first quarter of 2011, the Company granted 1,700,000 options with a fair value of \$0.7 million as determined by the Hull-White option pricing model using the assumptions of a weighted average exercise price \$0.75, risk free interest rates within a range of 2.89% to 3.32%, volatility rates of between 59.7% to 67.1% and an expected life of between 6 and 10 years. These options are only exercisable when the share price exceeds \$0.70 for 60 consecutive days on a volume weighted

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average price basis. All options outstanding that were granted prior to 2010 do not contain the minimum price requirement and continue to be valued under the Black-Scholes model.

At March 31, 2011 6,441,795 options were outstanding under the Company's Option Plan with a weighted average exercise price of \$0.70 per Common Share. During the first quarter of 2011, the Company recorded compensation expense of \$0.1 million (2010 - \$0.1 million) which has been credited to contributed surplus.

The Company also has a Deferred Share Unit Plan for directors and designated executive officers. Directors may elect to take a portion of their fees in the form of DSUs and executives may elect to take a portion of their annual incentive bonus in the form of DSUs. The number of DSUs allotted is determined by dividing the dollar portion of the bonus that the executive elected to take in DSUs by the weighted average price of the Company's Common Shares for the five business days prior to the issue notification date. During the first quarter of 2011 designated executive officers were allotted 201,300 DSUs at a price of \$0.77 per DSU and a further 4,953 DSUs were issue to a director at a price of \$1.06 per DSU. The cumulative number of DSUs outstanding at March 31, 2011 was 803,209 (December 31, 2010 - 596,956). During the first quarter of 2011, the Company recorded compensation expense for these DSUs of \$0.5 million (2010 - \$0.6 million), with a corresponding credit to accounts payable and accrued liabilities.

18. Commitments and Contingencies

(a) Long-term fibre supply agreements

Certain of the Company's fibre supply agreements with third parties have minimum volume requirements and may, in the case of a failure to supply the minimum volume, require the Company to conduct whole log chipping, source the deficiency from third parties at additional cost to the Company or pay the party to the fibre supply agreement a penalty calculated based on the provisions contained in the relevant agreement. Should Western take significant market related curtailments in its sawmills, the volume of chips produced is reduced and accordingly there is greater risk that the Company may not meet its contractual obligations.

The Company has not delivered the annual minimum chip volume for 2010 under certain long-term fibre supply contracts and is in discussions to resolve the shortfalls. With respect to one significant contract the Company and the other party to the contract are working on amending the contract, including the minimum chip volume requirements. Negotiations are progressing but at this time the Company is unable to determine if the amendment will be executed, or whether the party to the contract will act on its security.

In the first quarter of 2011, the Company negotiated various amendments to other long-term fibre supply agreements including the modification of minimum chip volume commitments. Based on chip and pulp log volumes supplied year-to-date, the Company anticipates satisfying annual fibre commitments for 2011.

(b) Storm damage

In late September, 2010, heavy rains and strong winds on the northwest of Vancouver Island triggered power outages, mudslides, road washouts and flooding. Certain logging areas were impacted by these severe storms with bridge and culvert damage, logging road washouts and slides in reforested areas. Work has commenced to repair the damage with expenditures of \$1.2 million incurred and recognized in net income (loss) in the period (\$1.0 million in the year to December 31, 2010 and a further \$0.2 million in the first quarter of 2011). There is still some uncertainty over the final estimates of the cost of damages resulting from the event. The current estimate of the insurable damages claim is approximately \$1.7 million which, as at March 31, 2011, has not been recognized in the Statement of Financial Position. It is anticipated there could be further uninsurable damages which have not yet been quantified but preliminary estimates are that they are not expected to exceed \$1.0 million. The impact on capitalized roads and bridges and other infrastructure is not expected to be significant.

(c) Lumber duties

On February 17, 2011, Canada issued a response to the request for arbitration made by the United States Trade Representative to the London Court of International Arbitration. This relates to allegations made by the United States of under-pricing of timber in the British Columbia interior region and

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circumvention of export measures provided for in the softwood lumber agreement (“SLA”) between Canada and the United States. The response by Canada was to refute the allegations, stating that the terms of the SLA had not been violated and that the United States’ claims were based on conjecture and without merit. A ruling from the London Court of International Arbitration is expected to take up to a year to be released. It is not possible to predict the outcome of the claims, or whether they would potentially have any impact on Western since they are specifically directed at British Columbia interior practices, and Western operates predominantly on the coast of British Columbia.

19. Financial Instruments

Certain of the Company’s sales transactions are denominated in foreign currencies, principally, the US dollar and Japanese Yen (“JPY”), and accordingly the Company is exposed to currency risk associated with changes in foreign exchange rates. To mitigate this foreign exchange risk, the Company entered into an agreement dated March 31, 2009 with BAM to provide a foreign exchange facility (“Facility”) to the Company. The Facility provides for a notional amount of up to US \$80.0 million, matures on March 31, 2012, and allows for forward transactions with a maximum term for each transaction of one year. The Facility automatically extends for one year on each anniversary date, provided that BAM has not notified the Company of its intention to cancel the facility at least 30 days prior to the anniversary date and subject to certain change of control provisions. The Facility is unsecured and is subject to an annual fee of 0.10% of the maximum notional amount. The Company does not consider the counter party credit risk associated with this Facility to be significant.

As at March 31, 2011, the Company had outstanding obligations to sell an aggregate JPY 4,460 million at an average rate of JPY 80.88 per CAD with maturities through December 30, 2011. All foreign currency gains or losses to March 31, 2011 have been recognized in revenue in net income (loss) for the period and the fair value of these instruments at March 31, 2011 was a net asset of \$2.5 million (December 31, 2010 - \$0.8 million) which is included in trade and other receivables on the Statement of Financial Position. A net gain of \$1.1 million was recognized on contracts which were settled in the first quarter of 2011 (2010 - \$ nil), which was included in revenue in net income (loss) for the period.

20. Operating Restructuring Items

Operating restructuring costs of \$0.3 million in the first quarter of 2011 relate to severance costs associated with restructuring administrative functions.

21. Other Income (Expenses)

Other expenses of \$0.5 million for the first quarter of 2011 comprised net losses on non-core asset sales of \$0.8 million, a gain on the sale of an equity interest in certain real estate properties of \$2.4 million (Note 8), an expense incurred of \$2.5 million to secure amendments to the terms of certain contractual arrangements, and other items totaling income of \$0.4 million. The most significant non-core asset sale in the quarter was the previously announced sale to TimberWest Forest Corp. of 7,678 hectares of land located in the southern portion of Vancouver Island near Jordan River for gross proceeds of \$21.9 million. In addition, during the quarter the Company exercised the option to sell its equity interest in WFPFPL, the entity that held the jointly owned entity established in 2009 between the Company and BPL, receiving \$2.4 million as consideration for the sale of its interest, and the right of first offer was extinguished (Note 8). The expense recognized in the first quarter of 2011 of \$2.5 million relating to the securing of amendments to certain existing contractual arrangements is payable in 14 equal quarterly installments commencing March 31, 2011.

In comparison, the first quarter of 2010 included other income of \$10.4 million. This amount primarily related to a receipt in January 2010 of \$8.9 million being the balance of the proceeds related to the establishment of the jointly-owned entity in 2009 with BPL, a company related to BAM (Note 8). Also included in other income was a re-imburement from the Province of British Columbia of \$0.9 million relating to prior-period stumpage re-assessments, and sundry other items totaling \$0.6 million.

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22. Expenses by Function

	Three months ended March 31	
	2011	2010
Administration	\$ 4.3	\$ 3.0
Distribution expenses	24.8	17.0
Cost of goods sold	149.7	115.6
	<u>\$ 178.8</u>	<u>\$ 135.6</u>

23. Other Expense Information

The Company recorded total employee compensation costs in the first quarter of 2011 of \$42.9 million (2010 - \$36.4 million). Total depreciation and amortization expense for the quarter was \$5.6 million (2010 - \$5.9 million).



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