# Western Forest Products Inc.

2015 First Quarter Report

Western Forest Products Inc.

## Letter to Shareholders

To Our Shareholders,

**Record first quarter log production and an improved lumber sales mix combined to deliver adjusted EBITDA of $29.6 million in the first quarter of 2015.**

Increased log sales volumes supported by Western's favourable log harvest in the first quarter, as well as improved lumber sales mix and the benefit of a weaker Canadian dollar ("CAD"), combined to double adjusted EBITDA from the fourth quarter of 2014.

Western successfully capitalized on favourable operating conditions to increase log harvest production by 14% compared to the same period last year. The increased supply of logs supported a 20% increase in log sales volumes compared to last year and an improved log supply to our sawmills. In addition, an improved lumber product sales mix and the benefit of a weaker CAD drove average realized lumber prices to their highest level in company history. The improved lumber pricing and increased log sales offset the continued weakness in export log and lumber markets and the slow start to the North American building season which has impacted commodity lumber consumption and pricing.

**First quarter 2015 financial highlights:**

- Increased adjusted EBITDA by $14.8 million from the prior quarter to $29.6 million
- Increased liquidity by $30.1 million to $164.5 million
- Returned $7.9 million to shareholders through the Company's quarterly dividend program
- Completed the sale of the Company's former Squamish pulp mill site for $21.8 million

**First quarter 2015 operational successes:**

- Delivered improved safety performance reducing our recordable incident rate
- Set a company record for highest first quarter log production volume at 1,472 Mm3
- Increased log sales volume by 20% from the first quarter last year to 700 Mm3
- Increased first quarter Western Red Cedar lumber sales volumes for the third consecutive year

**Demand for our specialty lumber and in particular Western Red Cedar ("WRC") and Niche products is expected to remain strong** during the second quarter supported by improved seasonal demand. A limited supply of WRC and continued strength in the US repair and renovation market should support pricing through 2015 and beyond.

**We anticipate that higher seasonal demand from US new home construction will positively impact commodity lumber pricing** as we move through the second quarter. We believe that Chinese lumber demand will stabilize at current levels while volumes to Japan are expected to increase moderately over the next two quarters. In the short-term, we anticipate continued price volatility in these markets until supply and demand come into closer balance in these markets.

**Strong demand for specialty log sorts in the domestic log market** and price pressures in export log markets should continue in the second quarter of 2015. High inventories in the China log market are expected to come into line, and may lead to higher export log pricing, in the second half of the year.

**We continue to invest in our coastal B.C. manufacturing base.** I am pleased to announce a further $30 million in strategic capital investments have been approved. The investments include another phase of our Duke Point sawmill modernization which we expect will deliver increased productivity and reduced costs of production for our lumber products. We will also be moving forward with the next phase of our Duke Point planer upgrade that will include the installation of the same autograding technology that we pioneered at Alberni Pacific.

**We take pride in our commitment to safety**, and it is encouraging to report that Western continues to be an industry leader in safety performance.

I would like to take this opportunity to thank our shareholders, customers, employees and the communities where we work for their continued support of Western Forest Products.

Sincerely,

**Don Demens**
*President and CEO*

# Management's Discussion & Analysis

The following Management's Discussion and Analysis ("MD&A") 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, 2015 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 financial statements for the three months ended March 31, 2015 and the audited annual consolidated financial statements and management's discussion and analysis for the year ended December 31, 2014 (the "2014 Annual Report"), all of which can be found on SEDAR at www.sedar.com.

The Company has prepared the unaudited condensed consolidated interim financial statements for the three months ended March 31, 2015 in accordance with IAS 34, *Interim Financial Reporting*, and these do not include all of the information required for full annual financial statements.

Reference is made in this MD&A to adjusted EBITDA[1] and adjusted EBITDA margin[2]. Adjusted EBITDA is defined as operating income prior to operating restructuring items and other income (expenses), plus amortization of property, plant, equipment and intangible assets, impairment adjustments, and changes in fair value of biological assets. Adjusted EBITDA margin is adjusted EBITDA as a proportion of revenue. Western uses adjusted EBITDA and adjusted EBITDA margin as benchmark measurements of our own operating results and as benchmarks relative to our competitors. We consider adjusted EBITDA to be a meaningful supplement to operating income as a performance measure primarily because amortization expense, impairment adjustments 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, the inclusion of operating restructuring items which are unpredictable in nature and timing may make comparisons of our operating results between periods more difficult. We also believe adjusted EBITDA and adjusted EBITDA margin are commonly used by securities analysts, investors and other interested parties to evaluate our financial performance.

Adjusted EBITDA does not represent cash generated from operations as defined by IFRSs and it is not necessarily indicative of cash available to fund cash needs. Furthermore, adjusted EBITDA does not reflect the impact of a number of items that affect our net income. Adjusted EBITDA and adjusted EBITDA margin are not measures of financial performance under IFRSs, and should not be considered as alternatives to measures of performance under IFRSs. Moreover, because all companies do not calculate adjusted EBITDA in the same manner, adjusted EBITDA and adjusted EBITDA margin calculated by Western may differ from similar measures calculated by other companies. A reconciliation between the Company's net income as reported in accordance with IFRSs and adjusted EBITDA is included in Appendix A to this report.

Also in this MD&A, management uses key performance indicators such as net debt, net debt to capitalization and current assets to current liabilities. Net debt is defined as long-term debt less cash and cash equivalents. Net debt to capitalization is a ratio defined as net debt divided by capitalization, with capitalization being the sum of net debt and shareholder's equity. Current assets to current liabilities is defined as total current assets divided by total current liabilities. These key performance indicators are non-GAAP financial measures that do not have a standardized meaning and may not be comparable to similar measures used by other issuers. They are not recognized by IFRSs; however, they are meaningful in that they indicate the Company's ability to meet their obligations on an ongoing basis, and indicate whether the Company is more or less leveraged than the prior periods.

This MD&A 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 our MD&A in the 2014 Annual 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.

Unless otherwise noted, the information in this discussion and analysis is updated to May 7, 2015. Certain prior period comparative figures have been reclassified to conform to the current period's presentation. All financial references are in millions of Canadian dollars unless otherwise noted.

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[1] Earnings Before Interest, Tax, Depreciation and Amortization

[2] Adjusted EBITDA as a proportion of Revenue

**Summary of Selected Quarterly Results[1]**

| *(millions of dollars except per share amount)* | Three months ended March 31, 2015 | Three months ended March 31, 2014 |
|---|---|---|
| Revenue | $ 248.6 | $ 246.0 |
| Adjusted EBITDA | 29.6 | 32.8 |
| Adjusted EBITDA margin | 11.9% | 13.3% |
| Operating income prior to restructuring items and other income | 20.1 | 24.9 |
| Net income from continuing operations | 18.5 | 23.6 |
| Net income for the period | 27.6 | 23.6 |
| Basic and diluted earnings per share (in dollars) - continuing operations | $ 0.05 | $ 0.06 |
| Basic and diluted earnings per share (in dollars) - discontinued operations | $ 0.02 | $ - |

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

(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.

## Overview

Western reported adjusted EBITDA of $29.6 million in the first quarter of 2015 on the strength of increased log shipments, buoyed by growth in log production volumes, and the revenue impact of a strengthening U.S. dollar ("USD"). Adjusted EBITDA decreased $3.2 million in comparison to the same period in 2014 due to challenging market conditions for lumber in Japan and logs and lumber in China, and slower than anticipated growth in the North American Commodity lumber market. These factors were partly offset by a reduction in selling and administration expense.

Revenue grew to $248.6 million in the first quarter of 2015, an improvement of $2.6 million over the same period last year. Increased log shipments, an improved lumber sales mix, and the benefit of a 12% weakening of the Canadian dollar ("CAD") relative to the USD contributed to these results.

First quarter lumber revenue remained flat despite lower lumber production and shipments compared to the same period in 2014. The benefit of a weaker Canadian dollar on lumber pricing was offset by market conditions in Japan and China that remain relatively unchanged from the second half of 2014. Continued strength from the North American repair and renovation sector led to increased demand for Western Red Cedar ("WRC") and Niche lumber products. We utilized our flexible operating platform and increased log production to direct greater volume to these high-value segments.

In the first quarter of 2015, log shipments increased 20%, yielding an 11% increase in log revenue compared to the same period in 2014. The benefit of a weaker CAD on export log revenue partially offset a significant decline in export prices and a lower quality domestic log sales mix as compared to the first quarter of 2014. Average export log realizations in the first quarter of 2015 were largely unchanged from the fourth quarter of 2014 primarily due to a weaker CAD relative to the USD.

Lumber production decreased 12% in the first quarter of 2015 compared to the same quarter of last year as we continued to implement changes in our operating platform to match production levels to market conditions, including reduced production from custom cut facilities. As compared to the fourth quarter of 2014, lumber production increased 3% which was achieved through our flexible production programs and through realizing the benefits of capital investments in our operations.

Exceptionally mild winter weather resulted in a 14% increase in first quarter log production volumes as compared to the same period in 2014. Log production costs remained flat period over period as increased road construction spending was offset by a reduction in fixed costs per cubic metre due to higher harvest volumes.

Net income for the first quarter of 2015 was $27.6 million, or $0.07 per common share, as compared to net income of $23.6 million, or $0.06 per common share, for the same period in 2014. Included in net income in the first quarter of 2015 is net income from discontinued operations of $9.1 million, recognized in relation to completing the sale of the former Squamish pulp mill site.

Total liquidity at March 31, 2015, has improved to $164.5 million, compared to $134.4 million at the end of 2014. The increased liquidity in 2015 was the result of cash generated by operations and the sale of non-core assets, offset by continued capital investment and dividends distributed to shareholders. In the first quarter of 2015, we continued to provide returns to our shareholders through our dividend program that returned $7.9 million, or $0.02 per common share, to shareholders on March 20, 2015.

## Operating Results

| *(millions of dollars)* | Three months ended March 31, 2015 | 2014 |
|---|---|---|
| Revenue | | |
| Lumber | $ 171.8 | $ 173.9 |
| Logs | $ 61.2 | 55.2 |
| By-products | $ 15.6 | 16.9 |
| Total revenue | 248.6 | 246.0 |
| Adjusted EBITDA | 29.6 | 32.8 |
| Adjusted EBITDA margin | 11.9% | 13.3% |

In the first quarter of 2015, we generated $248.6 million of revenue and $29.6 million of adjusted EBITDA compared to $246.0 million and $32.8 million, respectively, in the same quarter last year. Revenue results benefited from an increase in average lumber price driven by adjusting our sales mix and a weaker CAD, and increased log shipments period over period. The decline in adjusted EBITDA was primarily due to a weak price environment in the Chinese log and lumber market and lower volumes and prices in the Japan market, partly offset by a reduction in selling and administration expense.

Lumber revenue in the first quarter of 2015 of $171.8 million was flat relative to revenue in the same period of 2014. Average lumber prices increased $51 per thousand board feet, offsetting a 7% reduction in lumber volumes shipped, in the first quarter of 2015 as compared to the same period of 2014. Higher average pricing was due to a combination of a 7% increase in WRC shipments and a 21% increase in Niche product shipments period over period, offset partly by a steep decline in Commodity product pricing. Foreign exchange movement also contributed to realized price improvements in WRC, Niche and Japan lumber sales period over period.

First quarter log revenue of $61.2 million in 2015 was an increase of 11% over the same period in 2014. Increased log revenue was due to growth in export and domestic log sales volumes of 18% and 16% respectively, supported by our increased harvest volumes. Due to continued pricing pressures in Asian markets, export log prices were lower as compared to the first quarter of 2014, and that impact to revenue was partly offset by a weaker CAD. First quarter export log prices were stable in 2015 as compared to the fourth quarter of 2014 due to a weaker CAD, while average realized domestic log prices declined due to a lower quality sales mix in 2015. Pulp prices increased moderately over the first quarter of 2014 and held constant with pricing in the fourth quarter of 2014, while first quarter pulp shipment volumes increased from the same period of 2014 due to timing of sales.

By-products revenue was $15.6 million in the first quarter of 2015, a decrease of $1.3 million from the same period in 2014. This decrease in by-products revenue resulted from a 10% reduction in chip volumes sold due to decreased lumber production.

Lumber production in the first quarter of 2015 was 209 million board feet, a decrease of 12% as compared to the same quarter of 2014. This decrease resulted from the permanent closure of our Nanaimo sawmill in November 2014 and the internalization of some traditional custom cut production to match lumber production volumes to market conditions. Production from custom cut facilities is expected to gradually be reduced with the continued modernization and ramp-up of production at the Duke Point sawmill.

As compared to the fourth quarter 2014, lumber production in the first quarter of 2015 increased 3%, which was achieved through our flexible production programs and through realizing the benefits of capital investments in our operations.

Exceptionally mild winter weather in our timberlands operations allowed the Company to set a first quarter log production record in 2015 at approximately 1.5 million cubic metres. This log production volume represents a 14% increase from the first quarter of 2014, while our competitors' coastal harvest volumes declined by 15% according to the Province of British Columbia's Harvest Billing System. Our log production performance enabled increased log shipments while also building mill log inventory to support lumber production leading into the second quarter, a seasonally strong lumber sales period.

Our log production costs remained consistent with the first quarter of 2014 as the economies of scale realized through higher harvest volumes in 2015 were offset by increased road construction costs and the mix of harvest operations. These increased costs were the result of harvesting timber at higher elevations not historically accessible in the first quarter. Harvesting costs and log values are generally higher in this terrain. The mild winter weather also allowed the advancement of our 2015 road building plan in the first quarter of 2015, resulting in $2.9 million greater spur road construction expense as compared to the first quarter of 2014. By advancing our road building plan in the quarter we have increased our access to timber for future harvest and improved the flexibility of our harvest programs.

Freight costs were $20.8 million in the first quarter of 2015, an increase of $2.1 million compared to the same period of 2014. This increase was due to a 20% greater volume of log shipments and the weaker CAD relative to USD, the currency in which our freight costs are primarily denominated. Offsetting these factors were the favourable shift in geographic mix of lumber shipments and a reduction in fuel surcharges.

Selling and administration expense decreased by 34% from the first quarter of 2014 to $6.5 million in the first quarter of 2015. These savings were achieved partly due to reduced selling expenses and through various optimization initiatives launched in the second half of 2014, including the consolidation of our northern Vancouver Island timberlands operations, our Nanaimo-area manufacturing operations and our Japan sales offices. Also contributing to lower administration expense were reduced compensation costs.

First quarter net income was $27.6 million in 2015, as compared to $23.6 million in the same period in 2014. Increased net income reflects those circumstance presented above and includes net income from discontinued operations of $9.1 million arising from the completion of the sale of the Company's former Squamish pulp mill site in February 2015.

*Finance costs*

Finance costs in the first quarter of 2015 were $1.3 million, a decrease of $0.3 million compared to the same quarter of 2014. This decrease was commensurate with a reduction in interest rates and lower outstanding debt levels on our revolving term loan facility. The average debt balance outstanding in the first quarter of 2015 was $74.0 million as compared to $89.8 million in the same quarter of 2014.

*Discontinued Operations*

The sale of the Company's former Squamish pulp mill site was completed February 6, 2015 for cash proceeds of $21.8 million.

Included in net income of $9.1 million from discontinued operations for the first quarter of 2015 are a gain on disposal of property, plant and equipment; revenue from the sale of hydro-electric power generated at the site partly offset by site operating costs incurred up to the sale completion date; as well as a gain on reversal of a liability.

As economic and other circumstances allow, Western will continue to pursue opportunities to sell non-core assets.

## Financial Position and Liquidity

| *(millions of dollars except where noted)* | | Three months ended March 31, 2015 | | 2014 |
|---|---|---|---|---|
| Cash provided by operating activities, excluding non-cash working capital | $ | 28.8 | $ | 32.6 |
| Cash provided by operating activities | | 8.2 | | 20.4 |
| Cash used in investing activities | | (10.1) | | (8.2) |
| Cash used in financing activities | | (14.8) | | (8.1) |
| Cash used in capital logging roads | | (2.5) | | (3.4) |
| Cash used to acquire property, plant and equipment | | (7.6) | | (4.8) |

| | | March 31, 2015 | | December 31, 2014 |
|---|---|---|---|---|
| Total liquidity [1] | $ | 164.5 | $ | 134.4 |
| Net debt [2] | | 67.1 | | 77.9 |
| Financial ratios: | | | | |
| Current assets to current liabilities | | 2.40 | | 2.29 |
| Net debt to capitalization [3] | | 0.14 | | 0.16 |

(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

First quarter cash provided by operating activities, excluding changes in non-cash working capital items, amounted to $28.8 million in 2015 as compared to $32.6 million in the same quarter of 2014.

Including the change in non-cash working capital items, cash provided by operating activities in the first quarter of 2015 was $8.2 million as compared to $20.4 million in the same quarter of 2014, primarily due to the build-up of inventory period over period and an increase in trade accounts receivable due to the timing of sales. Mild winter weather conditions enabled the Company to achieve a record first quarter log production. Increased log production allowed for a greater inventory build-up period over period to position Western for the seasonally strong second quarter. The increase in non-cash working capital requirements was partly offset by an increase in accounts payable and accrued liabilities due to the timing of payments.

Cash used in investing activities was $10.1 million in the first quarter of 2015, compared to cash used in investing activities of $8.2 million in the same quarter of 2014. The Company expended $10.1 million in capital investments in the first quarter of 2015.

Capital investments in the first quarter of 2015 increased by 22% as compared to the first quarter of 2014, and were comprised of strategic capital investments of $4.8 million, discretionary spending on capital roads of $2.5 million, and other discretionary capital maintenance projects of $2.8 million. The strategic capital invested in the first quarter of 2015 primarily related to preparation for the log merchandiser installation project at Saltair which is scheduled to occur in the third quarter of 2015, and progress made on the Duke Point modernization project. Our strategic capital program is discussed in more detail in the "Strategy and Outlook" section.

In the first quarter of 2015, financing activities used cash of $14.8 million compared to the $8.1 million utilized in the same quarter of 2014. We returned $7.9 million, or $0.02 per common share, to shareholders on March 17, 2015, and repaid $6.7 million against our revolving credit facility during the first quarter of 2015.

Total liquidity was $164.5 million at March 31, 2015, an increase of $30.1 million over the first three months of 2015. The increase in liquidity was due to cash generated by operations, proceeds from the sale of non-core assets, and increased borrowing base under the revolving credit facility. At March 31, 2015, liquidity was comprised of cash of $6.0 million, unused availability under the secured revolving credit line of $122.5 million, and $36.0 million available under the revolving term loan facility.

## Strategy and Outlook

Western's strategy, which is designed to maximize product margins while increasing our sales volume, continued to progress in the first quarter of 2015.

Key operational priorities in support of our strategy include:

- Increasing log availability through improved log utilization
- Accessing additional log volume on the open market to increase lumber production
- Improving productivity through increased equipment utilization
- Focusing our lumber marketing programs by mill to drive higher margins

*Market Outlook*

The second quarter has historically produced the highest quarterly lumber sales volume, and we expect the same for 2015. Led by seasonally improved growth in U.S. new home construction and the impact of a tight log supply in the domestic market, we expect Commodity lumber demand and pricing to improve late in the second quarter. Our lumber shipments to the U.S. began to incur an export tax of 5% in April. Export taxes will remain in place until the commodity price index recovers.

We capitalized on mild winter weather in our timberlands operations in the first quarter by increasing log production and log inventories, including a proportionate increase in WRC log inventory. This harvest strategy has positioned us to continue to grow WRC lumber production and shipment volumes in the second quarter. Similarly, demand for our Niche products is anticipated to continue its upward trend during the second quarter, a time of increased demand in the U.S. repair and renovation market. We expect prices for WRC and Niche lumber products to remain firm.

Price pressures remain in the Japanese and Chinese lumber markets. Our focus for these markets continues to be the refinement of sales channels and managing near-term market conditions through our flexible operating platform, by directing production to the highest margin markets and products.

Combining our robust first quarter harvest volumes with prime harvesting conditions in the second quarter, our log inventory will enable us to optimize log supply to our sawmills while supporting log sales programs.

Demand from the domestic log market is expected to remain stable due to a 15% reduction in first quarter coastal BC harvest volumes by our competitors, a period in which Western increased log production by 14%. In addition, seasonal lumber demand improvements and an increase in U.S. building activity in the second quarter may positively influence pricing and demand for our domestic logs.

Export log pricing is expected to remain under pressure until inventories in China are consumed. Increased consumption of our log inventory in the second quarter will moderately reduce our exposure to any further decline in export log prices.

Pulp log market pricing is expected to remain flat as current market challenges including a coastal pulp mill curtailment, are expected to remain through 2015.

*Strategic Capital Plan Update*

Our strategic capital plan continues to make steady progress. During the first quarter of 2015, we advanced the Duke Point sawmill modernization project, including mill infrastructure improvements and made preparations for scheduled downtime in May 2015 for Phase II modernization upgrades.

To take advantage of the seasonally strong lumber market in the second quarter, other projects involving downtime at our operations including the log merchandiser installation at our Saltair sawmill have been deferred to the third quarter of 2015.

On May 7, 2015, we announced additional planned strategic capital investments of $30.0 million. Despite current market pressures, we are well positioned to pursue these capital investments as a result of our strong balance sheet and cash generated from operations. The upcoming capital investments in our operations are expected to increase productivity, reduce production costs, and increase margins from Western's continued harvest of its complete forest profile. On completing the strategic capital program, we expect to have improved our competitiveness and gained access to new markets.

## New accounting policies

*New standards and interpretations not yet adopted*

The following new and amended IFRS standards are not effective for the year ended December 31, 2015 and have not been applied in preparing these consolidated financial statements:

- IFRS 15, *Revenue from Contracts with Customers ("IFRS 15")*

  IFRS 15 is effective for years commencing on or after January 1, 2017, and will replace IAS 18, Revenue, IAS 11, Construction Contracts, and a number of revenue related interpretations. IFRS 15 provides a single, principles based five-step model to be applied to all contracts with customers, except insurance contracts, financial instruments, and lease contracts, which fall in the scope of other IFRSs. The Company intends to adopt IFRS 15 in its consolidated financial statements for the year commencing January 1, 2017. The extent of the impact of adoption of the standard has not yet been determined.

- IFRS 9, *Financial Instruments ("IFRS 9")*

  IFRS 9 is effective for years commencing on or after January 1, 2018, and will replace IAS 39, Financial Instruments: Recognition and Measurement. Under IFRS 9, financial assets will be classified and measured based on the business model in which they are held and the characteristics of the associated contractual cash flows. IFRS 9 also includes a new general hedge accounting standard which will better align hedge accounting with risk management. The Company intends to adopt IFRS 9 in its consolidated financial statements for the year commencing January 1, 2018; the extent of the impact of adoption of the amendments has not yet been determined.

- *Annual improvements to IFRS*

  The IASB issued narrow-scope amendments to various standards as part of its annual improvements process in December 2014. The IASB uses the annual improvements process to make non-urgent but necessary amendments to IFRS. Most amendments apply prospectively for annual periods beginning on or after January 1, 2016; earlier application is permitted, in which case, the related consequential amendments to other IFRSs would also apply. Amendments were made to clarify the following in their respective standards:

  - Definition of "continuing involvement" in IFRS 7, Financial instruments: Disclosures;
  - Discount rates for post-employment benefit obligations in IAS 19, Employee Benefits; and,
  - Disclosure requirements in IAS 34, Interim financial reporting.

  The Company intends to adopt these amendments in its financial statements for the annual period beginning on January 1, 2016. The extent of the impact of adoption of the amendments has not yet been determined.

The following revised IFRSs became effective on or after January 1, 2015. However, they do not have a material impact on the annual consolidated financial statements of the Company:

- IFRS 8, *Operating segments*
- IAS 24, *Related party transactions*

## Risks and Uncertainties

The business of the Company is subject to a number of risks and uncertainties, including those described in the 2014 Annual Report which can be found on SEDAR, at www.sedar.com. Any of the risks and uncertainties described in the above-noted document could have a material adverse effect on our operations and financial condition and cash flows and, accordingly, should be carefully considered in evaluating Western's business.

## Evaluation of Disclosure Controls and Procedures

As required by National Instrument 52-109 issued by the Canadian Securities Administrators, Western conducted an evaluation of the effectiveness of the disclosure controls and procedures and internal controls over financial reporting based on the "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company's system of internal control over financial reporting was effective as at December 31, 2014. 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 were 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 were 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.

The CEO and CFO confirm that 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 2015.

## Outstanding Share Data

As of May 7, 2015, there were 395,065,407 common shares issued and outstanding.

Western has reserved 20,000,000 common shares for issuance upon the exercise of options granted under the Company's incentive stock option plan. During the three months ended March 31, 2015, 266,000 previously granted options were exercised, and 1,491,667 options were granted. On May 7, 2015, 11,656,667 options were outstanding under the Company's incentive stock option plan.

## Management's Discussion and Analysis – Appendix A

Summary of Selected Results for the Last Eight Quarters

| *(millions of dollars except per share amounts and where noted)* | 2015 | 2014 | | | | 2013 | | |
|---|---|---|---|---|---|---|---|---|
| | 1st | 4th | 3rd | 2nd | 1st | 4th | 3rd | 2nd |
| **Average Exchange Rate – Cdn $ to purchase one US $** | 1.241 | 1.136 | 1.089 | 1.091 | 1.103 | 1.049 | 1.039 | 1.023 |
| **Revenue** | | | | | | | | |
| Lumber | 171.8 | 166.8 | 180.4 | 207.9 | 173.9 | 168.1 | 171.7 | 180.4 |
| Logs | 61.2 | 51.2 | 66.0 | 71.8 | 55.2 | 59.7 | 53.9 | 67.0 |
| By-products | 15.6 | 14.6 | 15.7 | 16.5 | 16.9 | 14.2 | 13.8 | 14.9 |
| Total revenue | 248.6 | 232.6 | 262.1 | 296.2 | 246.0 | 242.0 | 239.4 | 262.3 |
| **Lumber** | | | | | | | | |
| Production – millions of board feet | 209 | 202 | 231 | 237 | 237 | 213 | 223 | 230 |
| Shipments – millions of board feet | 202 | 215 | 220 | 255 | 218 | 222 | 228 | 231 |
| Price – per thousand board feet | 849 | 775 | 820 | 815 | 798 | 758 | 752 | 782 |
| **Logs** | | | | | | | | |
| Production – thousands of cubic metres | 1,472 | 1,281 | 1,009 | 1,544 | 1,293 | 1,314 | 1,233 | 1,495 |
| Shipments – thousands of cubic metres | 700 | 571 | 707 | 773 | 581 | 697 | 615 | 765 |
| Price – per cubic metre (1) | 83 | 90 | 86 | 90 | 95 | 84 | 83 | 84 |
| **Selling and administration** | 6.5 | 6.0 | 8.3 | 8.1 | 9.8 | 8.8 | 8.2 | 8.0 |
| **Adjusted EBITDA** | 29.6 | 14.8 | 20.0 | 40.9 | 32.8 | 24.4 | 27.6 | 44.9 |
| Amortization | (7.8) | (6.7) | (7.0) | (8.2) | (7.7) | (7.0) | (7.5) | (7.9) |
| Changes in fair value of biological assets | (1.7) | 0.5 | (0.4) | (1.4) | (0.2) | (0.7) | (0.3) | (0.8) |
| Reversal of impairment | - | 2.9 | - | - | - | 8.2 | - | - |
| Operating restructuring items | (0.3) | (1.2) | (8.3) | (1.2) | (0.1) | (0.1) | (0.3) | (0.1) |
| Finance costs | (1.3) | (1.2) | (1.4) | (1.5) | (1.6) | (1.7) | (1.7) | (0.8) |
| Other income (expenses) | 0.1 | 0.6 | - | 0.6 | 0.2 | (0.1) | (0.4) | 0.7 |
| Deferred income tax recovery | 0.1 | 3.2 | - | - | 0.2 | 26.5 | - | - |
| Current income tax recovery (expense) | (0.2) | (0.0) | (0.2) | - | - | 0.4 | (0.2) | (0.3) |
| **Net income from continuing operations** | 18.5 | 12.9 | 2.7 | 29.2 | 23.6 | 49.9 | 17.2 | 35.7 |
| Net income (loss) from discontinued operations | 9.1 | - | - | - | - | - | - | (0.2) |
| **Net income** | 27.6 | 12.9 | 2.7 | 29.2 | 23.6 | 49.9 | 17.2 | 35.5 |
| Adjusted EBITDA margin | 11.9% | 6.4% | 7.6% | 13.8% | 13.3% | 10.1% | 11.5% | 17.1% |
| Earnings per share: | | | | | | | | |
| Net income, basic | 0.07 | 0.03 | 0.01 | 0.07 | 0.06 | 0.13 | 0.04 | 0.08 |
| Net income, diluted | 0.07 | 0.03 | 0.01 | 0.07 | 0.06 | 0.13 | 0.04 | 0.07 |

(1) The log revenue used to determine average price per cubic metre has been reduced by the associated shipping costs arranged in the respective periods to enable comparability of unit prices.

In a normal operating year there is seasonality to the Company's operations with higher lumber sales in the first half through to early in the third quarter when construction activity, particularly in 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.

Certain categories of transactions are presented separately above due to their unpredictable timing and to allow for greater comparability of our operating results between periods. In the first quarter of 2015, the Company recognized $9.1 million net income from discontinued operations relating to its former Squamish pulp mill site that was sold on February 6, 2015. The third quarter of 2014 included an $8.1 million restructuring provision related to the consolidation of its Nanaimo sawmill operations. The fourth quarters of 2014 and 2013 include impairment reversals of $2.9 million and $8.2 million, respectively, that had been taken on the Company's timber licenses (intangible assets). In the fourth quarters of 2014 and 2013, the Company recognized deferred income tax assets of $3.2 million and $26.5 million, respectively, with respect to unutilized operating tax losses.

## Western Forest Products Inc.

Unaudited Condensed Consolidated Interim Financial Statements

For the three months ended March 31, 2015 and 2014

**Western Forest Products Inc.**
**Condensed Consolidated Statements of Financial Position**
*(Expressed in millions of Canadian dollars) (unaudited)*

| | March 31, 2015 | December 31, 2014 |
|---|---|---|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | $ 6.0 | $ 1.8 |
| Trade and other receivables | 83.1 | 65.6 |
| Inventory (Note 5) | 160.3 | 139.4 |
| Prepaid expenses and other assets | 12.0 | 8.8 |
| | 261.4 | 215.6 |
| Non-current assets: | | |
| Property, plant and equipment (Note 6) | 239.7 | 249.3 |
| Intangible assets (Note 6) | 128.3 | 129.3 |
| Biological assets (Note 7) | 55.2 | 56.9 |
| Other assets | 10.1 | 13.2 |
| Deferred income tax assets | 30.0 | 29.9 |
| | $ 724.7 | $ 694.2 |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | $ 98.9 | $ 76.6 |
| Revolving credit facility (Note 8) | - | 6.7 |
| Silviculture provision (Note 11) | 9.8 | 10.7 |
| Discontinued operations (Note 16) | - | 0.3 |
| | 108.7 | 94.3 |
| Non-current liabilities: | | |
| Long-term debt (Note 9) | 73.1 | 73.0 |
| Silviculture provision (Note 11) | 20.0 | 19.0 |
| Other liabilities (Note 10) | 35.1 | 32.9 |
| Deferred revenue | 61.9 | 62.4 |
| Discontinued operations (Note 16) | - | 4.5 |
| | 298.8 | 286.1 |
| Shareholders' equity: | | |
| Share capital - voting shares (Note 12) | 505.2 | 504.4 |
| Contributed surplus | 7.2 | 7.0 |
| Deficit | (86.5) | (103.3) |
| | 425.9 | 408.1 |
| | $ 724.7 | $ 694.2 |

Commitments and Contingencies (Note 13)

See accompanying notes to these unaudited condensed consolidated interim financial statements

Approved on behalf of the Board:

"Lee Doney"
Chairman

"Don Demens"
President and CEO

# 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, 2015 | 2014 |
|---|---|---|
| Revenue | $ 248.6 | $ 246.0 |
| Cost and expenses: | | |
| Cost of goods sold | 201.2 | 192.6 |
| Freight | 20.8 | 18.7 |
| Selling and administration | 6.5 | 9.8 |
| | 228.5 | 221.1 |
| **Operating income prior to restructuring items and other income** | 20.1 | 24.9 |
| Operating restructuring items | (0.3) | (0.1) |
| Other income | 0.1 | 0.2 |
| **Operating income** | 19.9 | 25.0 |
| Finance costs | (1.3) | (1.6) |
| **Income before income taxes** | 18.6 | 23.4 |
| Current income tax expense | (0.2) | - |
| Deferred income tax recovery | 0.1 | 0.2 |
| **Net income from continuing operations** | 18.5 | 23.6 |
| **Net income from discontinued operations** (Note 16) | 9.1 | - |
| **Net income** | 27.6 | 23.6 |
| **Other comprehensive loss** | | |
| Items that will not be reclassified to profit or loss: | | |
| Defined benefit plan actuarial loss | (2.9) | (2.4) |
| **Total comprehensive income** | $ 24.7 | $ 21.2 |
| Net income per share (in dollars): | | |
| Basic and diluted earnings per share | $ 0.07 | $ 0.06 |
| Basic and diluted earnings per share - continuing operations | $ 0.05 | $ 0.06 |
| Basic and diluted earnings per share - discontinued operations | $ 0.02 | $ - |
| Weighted average number of common shares outstanding (thousands) | | |
| Basic | 394,966 | 391,358 |
| Diluted | 399,615 | 399,150 |

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 | Deficit | **Total Equity** |
|---|---|---|---|---|
| **Balance at December 31, 2013** | $ 499.7 | $ 6.5 | $ (123.8) | $ 382.4 |
| Net income | - | - | 23.6 | 23.6 |
| Other comprehensive loss: | | | | |
| Defined benefit plan actuarial loss recognized | - | - | (2.4) | (2.4) |
| **Total comprehensive income** | - | - | 21.2 | 21.2 |
| Share-based payment transactions recognized in equity | - | 0.5 | - | 0.5 |
| Exercise of stock options | 0.7 | (0.2) | - | 0.5 |
| Dividends | - | - | (7.8) | (7.8) |
| **Total transactions with owners, recorded directly in equity** | 0.7 | 0.3 | (7.8) | (6.8) |
| **Balance at March 31, 2014** | $ 500.4 | $ 6.8 | $ (110.4) | $ 396.8 |

| | | | | |
|---|---|---|---|---|
| **Balance at December 31, 2014** | $ 504.4 | $ 7.0 | $ (103.3) | $ 408.1 |
| Net income | - | - | 27.6 | 27.6 |
| Other comprehensive loss: | | | | |
| Defined benefit plan actuarial loss recognized | - | - | (2.9) | (2.9) |
| **Total comprehensive income** | - | - | 24.7 | 24.7 |
| Share-based payment transactions recognized in equity | - | 0.4 | - | 0.4 |
| Exercise of stock options | 0.8 | (0.2) | - | 0.6 |
| Dividends | - | - | (7.9) | (7.9) |
| **Total transactions with owners, recorded directly in equity** | 0.8 | 0.2 | (7.9) | (6.9) |
| **Balance at March 31, 2015** | $ 505.2 | $ 7.2 | $ (86.5) | $ 425.9 |

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, 2015 | Three months ended March 31, 2014 |
|---|---|---|
| Cash provided by (used in): | | |
| Operating activities: | | |
| Net income from continuing operations | $ 18.5 | $ 23.6 |
| Items not involving cash: | | |
| Amortization of property, plant and equipment (Note 6) | 6.8 | 6.7 |
| Amortization of intangible assets (Note 6) | 1.0 | 1.0 |
| Change in fair value of biological assets (Note 7) | 1.7 | 0.2 |
| Net finance costs | 1.3 | 1.6 |
| Deferred income tax recovery | (0.1) | (0.2) |
| Other | (0.4) | (0.3) |
| | 28.8 | 32.6 |
| Changes in non-cash working capital items: | | |
| Trade and other receivables | (17.5) | (9.5) |
| Inventory | (20.9) | (13.9) |
| Prepaid expenses and other assets | (3.2) | (2.2) |
| Silviculture provision | (0.9) | (1.0) |
| Accounts payable and accrued liabilities | 21.9 | 14.4 |
| | (20.6) | (12.2) |
| | 8.2 | 20.4 |
| Investing activities: | | |
| Additions to property, plant and equipment (Note 6) | (10.1) | (8.2) |
| | (10.1) | (8.2) |
| Financing activities: | | |
| Interest paid | (0.8) | (0.8) |
| Repayment of revolving credit facility | (6.7) | - |
| Dividends | (7.9) | (7.8) |
| Proceeds from exercise of stock options | 0.6 | 0.5 |
| | (14.8) | (8.1) |
| Cash provided by continuing operations | (16.7) | 4.1 |
| Proceeds on disposal of assets | 21.8 | - |
| Other | (0.9) | - |
| Cash provided by discontinued operations (Note 16) | 20.9 | - |
| Increase in cash and cash equivalents | 4.2 | 4.1 |
| Cash and cash equivalents, beginning of period | 1.8 | 5.6 |
| Cash and cash equivalents, end of period | $ 6.0 | $ 9.7 |

See accompanying notes to these unaudited condensed consolidated interim financial statements

## 1. Reporting entity

Western Forest Products Inc. ("Western" or the "Company") is an integrated softwood forest products company, incorporated and domiciled in Canada, operating in the coastal region of British Columbia. The address of the Company's registered office is Suite 510 – 700 West Georgia Street, Vancouver, British Columbia, Canada. The unaudited condensed consolidated interim financial statements as at and for the three months ended March 31, 2015 and 2014 comprise 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 25 countries worldwide. The Company is listed on the Toronto Stock Exchange, under the symbol WEF.

## 2. Basis of preparation

*(a) Statement of compliance*

These unaudited condensed consolidated interim financial statements ("interim financial statements") have been prepared in accordance with IAS 34, *Interim Financial Reporting* ("IAS 34"). Selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in financial position and performance of the Company since the last annual consolidated financial statements as at and for the year ended December 31, 2014. These interim financial statements do not include all the information required for full annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRSs").

These interim financial statements were approved by the Board of Directors on May 7, 2015.

*(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;
- Liabilities for cash-settled share-based payment transactions are measured at fair value at each reporting period;
- Equity-settled share-based payments are measured at fair value at grant date;
- Derivative financial instruments are measured at fair value at each reporting date;
- The defined benefit pension liability is recognized as the net total of the fair value of the plan assets, less the present value of the defined benefit obligation; and
- Reforestation obligations are measured at the discounted value of expected future cash flows.

*(c) Functional and presentation currency*

These interim financial statements are presented in the Canadian dollar which is the Company's functional currency. All amounts are presented in millions of Canadian dollars, unless otherwise indicated.

*(d) Use of estimates and judgements*

The preparation of interim consolidated financial statements in accordance with IAS 34 requires Management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively.

## 2. Basis of preparation (continued)

*(d) Use of estimates and judgements (continued)*

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 the Company's annual consolidated financial statements as at and for the year ended December 31, 2014.

## 3. Significant accounting policies

The accounting policies applied by the Company in these interim financial statements are the same as those applied by the Company in its annual consolidated financial statements as at and for the year ended December 31, 2014, except for the adoption of revised standards as described below:

*(a) Changes in accounting policies*

Effective January 1, 2015, the Company has applied the following revised standards and interpretive guidance:

IFRS 8, *Operating segments*

This standard was amended to require disclosure of judgements made by management in aggregating segments, and a reconciliation of segment assets to the entity's assets when segment assets are reported. The application of this revised standard has not materially impacted the interim financial statements.

IAS 24, *Related party transactions*

This standard was amended to revise the definition of "related party" to include an entity that provides key management personnel services to the reporting entity or its parent, and to clarify related disclosure requirements. The application of this revised standard has not materially impacted the interim financial statements.

*(b) Standards and interpretations not yet effective*

IFRS 15, *Revenue from Contracts with Customers* ("IFRS 15")

IFRS 15 is effective for years commencing on or after January 1, 2017, and will replace IAS 18, *Revenue*, IAS 11, *Construction Contracts*, and a number of revenue related interpretations. IFRS 15 provides a single, principles based five-step model to be applied to all contracts with customers, except insurance contracts, financial instruments, and lease contracts, which fall in the scope of other IFRSs. The Company intends to adopt IFRS 15 in its consolidated financial statements for the year commencing January 1, 2017. The extent of the impact of adoption of the standard has not yet been determined.

IFRS 9, *Financial Instruments* ("IFRS 9")

IFRS 9 is effective for years commencing on or after January 1, 2018, and will replace IAS 39, *Financial Instruments: Recognition and Measurement*. Under IFRS 9, financial assets will be classified and measured based on the business model in which they are held and the characteristics of the associated contractual cash flows. IFRS 9 also includes a new general hedge accounting standard which will better align hedge accounting with risk management. The Company intends to adopt IFRS 9 in its consolidated financial statements for the year commencing January 1, 2018. The extent of the impact of adoption of the amendments has not yet been determined.

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 3. Significant accounting policies (continued)

*Annual improvements to IFRS*

The International Accounting Standards Board ("IASB") issued narrow-scope amendments to various standards as part of its annual improvement process in December 2014. The IASB uses the annual improvements process to make non-urgent but necessary amendments to IFRS. Most amendments apply prospectively for annual periods beginning on or after January 1, 2016; earlier application is permitted, in which case, the related consequential amendments to other IFRSs would also apply. Amendments were made to clarify the following in their respective standards:

- Definition of "continuing involvement" in IFRS 7, *Financial instruments: Disclosures*;
- Discount rates for post-employment benefit obligations in IAS 19, *Employee Benefits*; and,
- Disclosure requirements in IAS 34, *Interim financial reporting*.

The Company intends to adopt these amendments in its financial statements for the annual period beginning on January 1, 2016. The extent of the impact of adoption of these amendments has not yet been determined.

## 4. 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.

## 5. Inventory

| | March 31, 2015 | December 31, 2014 |
|---|---|---|
| Logs | $ 116.4 | $ 101.3 |
| Lumber | 45.7 | 38.9 |
| Supplies and other inventory | 11.7 | 11.4 |
| Provision for write downs | (13.5) | (12.2) |
| Total value of inventory | $ 160.3 | $ 139.4 |
| Inventory carried at net realizable value | $ 66.8 | $ 39.8 |

The Company's logs and lumber inventory is pledged as security against the revolving credit facility.

During the three months ended March 31, 2015, $201.2 million (2014: $192.6 million) of inventory was charged to cost of goods sold. This includes an increase to the provision for write-down to net realizable value of $1.3 million for the three months ended March 31, 2015 (2014: decrease of $0.5 million).

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 6. Property, plant and equipment and intangible assets

| Cost | Buildings & equipment | Logging roads | Land | Total property, plant & equipment | Intangible assets |
|---|---|---|---|---|---|
| Balance at January 1, 2014 | $ 190.5 | $ 137.8 | $ 103.8 | $ 432.1 | $ 170.9 |
| Additions | 36.4 | 13.5 | - | 49.9 | - |
| Disposals | (1.9) | - | (0.1) | (2.0) | (0.2) |
| Impairments | (10.6) | - | - | (10.6) | - |
| **Balance at December 31, 2014** | $ 214.4 | $ 151.3 | $ 103.7 | $ 469.4 | $ 170.7 |
| Additions | 7.6 | 2.5 | - | 10.1 | - |
| Disposals | (0.6) | - | (12.8) | (13.4) | - |
| **Balance at March 31, 2015** | $ 221.4 | $ 153.8 | $ 90.9 | $ 466.1 | $ 170.7 |
| | | | | | |
| **Accumulated amortization and impairments** | | | | | |
| Balance at January 1, 2014 | $ 100.6 | $ 105.5 | $ - | $ 206.1 | $ 40.4 |
| Amortization | 12.4 | 13.3 | - | 25.7 | 3.9 |
| Disposals | (1.6) | - | - | (1.6) | - |
| Impairments | (10.1) | - | - | (10.1) | - |
| Reversal of impairments | - | - | - | - | (2.9) |
| **Balance at December 31, 2014** | $ 101.3 | $ 118.8 | $ - | $ 220.1 | $ 41.4 |
| Amortization | 3.3 | 3.5 | - | 6.8 | 1.0 |
| Disposals | (0.5) | - | - | (0.5) | - |
| **Balance at March 31, 2015** | $ 104.1 | $ 122.3 | $ - | $ 226.4 | $ 42.4 |
| | | | | | |
| **Carrying amounts** | | | | | |
| At December 31, 2014 | $ 113.1 | $ 32.5 | $ 103.7 | $ 249.3 | $ 129.3 |
| At March 31, 2015 | $ 117.3 | $ 31.5 | $ 90.9 | $ 239.7 | $ 128.3 |

Total amortization expense for the three months ended March 31, 2015 was $7.8 million (2014: $7.7 million).

## 7. Biological assets

*(a) Reconciliation of carrying amount*

| | Three months ended March 31, 2015 | 2014 |
|---|---|---|
| Carrying value, beginning of period | $ 56.9 | $ 58.4 |
| Change in fair value resulting from growth and pricing | 0.8 | 0.8 |
| Harvested timber transferred to inventory in the period | (2.5) | (1.0) |
| Carrying value, end of period | $ 55.2 | $ 58.2 |

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 reporting date. The land underlying the standing timber is considered a component of property, plant and equipment, and is recorded at cost less accumulated impairment.

At March 31, 2015, private timberlands comprised an area of approximately 23,293 hectares (December 31, 2014: 23,293 hectares) of land owned by the Company; standing timber on these timberlands ranged from newly planted cut-blocks to old-growth forests. During the three months ended March 31, 2015, the Company harvested and scaled approximately 111,618 cubic metres of logs from its private timberlands, which had a fair value less costs to sell of $11.1 million at the date of harvest (2014: 79,102 cubic metres and $7.9 million, respectively).

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.

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 7. Biological assets (continued)

*(b) Measurement of fair values*

The fair value measurements for the Company's standing timber of $55.2 million has been categorized as Level 3 fair value based on the inputs to the valuation technique used (December 31, 2014: Level 3 fair value). The valuation technique used is discounted cash flows combined with market comparison.

At each interim reporting date, the Company examines market and asset conditions to determine if changing conditions would yield a change in fair value less costs to sell. The Company reviewed the underlying assumptions impacting its standing timber as at March 31, 2015 and noted no indication that a full re-assessment of fair value less costs to sell or the significant unobservable inputs was warranted at that date.

The change in fair value resulting from price and growth is reflected in cost of goods sold.

## 8. Revolving credit facility

The Company's revolving credit facility (the "Facility") 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 0.50% (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 interest rate for the Facility was 3.50% at March 31, 2015 (December 31, 2014: 3.50%).

The Facility is secured by a first lien interest over accounts receivable and inventory and includes financial covenants. At March 31, 2015, the Facility was unutilized (December 31, 2014: $6.7 million) and $122.5 million of the facility was available to the Company. The Facility matures on December 14, 2015, subject to any future refinancing requirements of its revolving term loan.

The Company was in compliance with its financial covenants at March 31, 2015.

## 9. Long-term debt

The Company's revolving term loan facility (the "Term Loan") provides for a maximum borrowing amount of $110.0 million and has a maturity date of June 29, 2019. The Term Loan bears interest at an index rate, determined as the higher of (i) the Canadian Prime rate plus 0.15%, and (ii) the 30 day Banker's Acceptance rate plus 1.65%. The interest rate for the Term Loan was 2.72% at March 31, 2015 (December 31, 2014: 2.92%).

The Term Loan is secured by a first lien interest over all of the Company's properties and assets, excluding those of the Englewood Logging Division and all accounts receivable and inventory, over which it has second lien interests, and includes financial covenants.

The Company was in compliance with its financial covenants at March 31, 2015.

| | March 31, 2015 | December 31, 2014 |
|---|---|---|
| Long-term debt | $ 74.0 | $ 74.0 |
| Less transaction costs | (0.9) | (1.0) |
| | $ 73.1 | $ 73.0 |

Transaction costs are deferred and being amortized to finance costs over the term of the Term Loan using the effective interest rate method.

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 10. Other liabilities

| | March 31, 2015 | December 31, 2014 |
|---|---|---|
| Employee future benefits obligation (Note 14) | $ 33.1 | $ 30.9 |
| Environmental accruals | 1.5 | 1.5 |
| Other | 0.5 | 0.5 |
| | $ 35.1 | $ 32.9 |

## 11. Silviculture provision

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

| | March 31, 2015 | March 31, 2014 |
|---|---|---|
| Silviculture provision, beginning of period | $ 29.7 | $ 30.0 |
| Silviculture provision charged | 3.1 | 2.6 |
| Silviculture work payments | (3.0) | (2.4) |
| Unwind of discount | - | 0.1 |
| Silviculture provision, end of period | 29.8 | 30.3 |
| Less current portion | 9.8 | 11.3 |
| | $ 20.0 | $ 19.0 |

The silviculture expenditures are expected to occur over the next one to ten years and have been discounted at risk-free rates of 0.50% to 1.36%. The total undiscounted amount of the estimated future expenditures required to settle the silviculture obligation at March 31, 2015 is $30.8 million (December 31, 2014: $30.9 million). Reforestation expense incurred on current production is included in production costs and the unwinding of discount, or accretion cost, is included in finance costs for the year.

## 12. Share capital

*(a) Issued and outstanding share capital*

| | Number of Common Shares | Amount |
|---|---|---|
| **Balance at December 31, 2014** | 394,799,407 | $ 504.4 |
| Exercise of stock options | 266,000 | 0.8 |
| **Balance at March 31, 2015** | 395,065,407 | $ 505.2 |

There were no Non-Voting shares outstanding at March 31, 2015.

*(b) 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 20,000,000 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 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 2015, the Company granted 1,491,667 options with a fair value of $0.6 million as determined by the Black-Scholes option pricing model using the assumptions of a weighted average exercise price of $2.20 per share, risk free interest rate of 0.97%, a volatility rate of 41.1%, and an expected life of seven years. These options are only exercisable when the share price has been equal to or exceeds $0.70 for the 60 consecutive days preceeding the date of exercise on a volume weighted average price basis. At March 31, 2015, 11,656,667 options were outstanding under the Company's Option Plan, with a weighted average exercise price of $1.45 per share.

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 12. Share capital (continued)

*(c) Deferred share unit plan*

The Company has a Deferred Share Unit ("DSU") Plan for directors and designated executive officers. Directors may elect to take a portion of their fees in the form of DSUs. All DSU holders are entitled to DSU dividends, equivalent to the dividend they would have received if they held their DSUs as shares. For directors, the number of DSUs allotted is determined by dividing the dollar portion of the quarterly fees a director elects to take in DSUs by the share price value on the fifth day following each quarter end. For executive officers, the number of DSUs allotted is determined by dividing the dollar portion of the bonus that an executive elects 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. For dividends, the number of DSUs allotted is determined by dividing the total dollar value of the dividend each DSU holder would have received, by the average share price for the five days leading up to the dividend date of record.

During the first quarter of 2015, 16,402 DSUs were issued at a price of $1.89 per DSU to certain directors who have elected to take a portion of their directors' fees in the form of DSUs. In addition, 2,450 DSUs and 4,297 DSUs were issued to designated executive officers and a director, respectively, at a price of $2.19 per DSU to reflect the cash dividend declared on Common Shares during the quarter. Furthermore, 43,262 DSUs were redeemed for cash by an executive. The cumulative number of DSUs outstanding at March 31, 2015 was 906,576 (December 31, 2014: 926,689).

During the three months ended March 31, 2015, the Company recorded a compensation recovery for these DSUs of $0.6 million (2014: compensation expense of $0.6 million), with corresponding decrease (2014: increase) to accounts payable and accrued liabilities.

## 13. Commitments and contingencies

*Long-term fibre supply agreements*

Certain of the Company's long term fibre supply agreements with third parties have minimum volume requirements and may, in the case of a failure to produce the minimum annual 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, if it is not possible to secure replacement chips on the open market during that period.

The Company had met all fibre commitments as at December 31, 2014 and based on chip and pulp log volumes supplied year-to-date, the Company anticipates satisfying annual fibre commitments for 2015.

## 14. Employee future benefits

The Company's salaried pension and non-pension benefits expense is as follows:

| | Three months ended March 31, 2015 | Three months ended March 31, 2014 |
|---|---|---|
| Current service costs | $ 0.1 | $ 0.1 |
| Net interest | 0.2 | 0.2 |
| Cost of defined benefit plans | 0.3 | 0.3 |
| Cost of defined contribution plans | 0.5 | 0.8 |
| Total cost of employee post-retirement benefits | $ 0.8 | $ 1.1 |

The amounts recognized in the statement of financial position for the Company's employee future benefit obligations, consisting of both the defined benefit salaried pension plans and other non-pension benefits are as follows:

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 14. Employee future benefits (continued)

| | March 31, 2015 | December 31, 2014 |
|---|---|---|
| Present value of obligations | $ (146.7) | $ (140.9) |
| Fair value of plan assets | 113.6 | 110.0 |
| Liability recognized in the statement of financial position (Note 10) | $ (33.1) | $ (30.9) |

The change in the liability recognized in the statement of financial position at March 31, 2015 was due primarily to the increased actuarial losses resulting from estimated changes in the discount rate used to value the defined benefit obligations partly offset by return on plan assets for the quarter. The discount rate used as at March 31, 2015 was 3.43% per annum, a decrease of 0.40% per annum from the rate used at December 31, 2014 of 3.83% per annum, and the return on assets over the three months to March 31, 2015 was 4.3% per annum.

The Company expects to make funding contributions to its defined benefit plans of $3.7 million during 2015.

## 15. Financial instruments – fair values

The following table shows the carrying amounts and fair values of financial assets and financial liabilities, including their levels in the fair valuation hierarchy. It does not include fair value information for financial assets or liabilities not measured at fair value if the carrying amount is a reasonable approximation of fair value. There has been no movement between fair value levels since December 31, 2014.

| | Carrying Amount | | | | | Fair Value | | | |
|---|---|---|---|---|---|---|---|---|---|
| **March 31, 2015** | Held to maturity | Designated at fair value | Loans and receivables | Other financial liabilities | **Total** | Level 1 | Level 2 | Level 3 | **Total** |
| **Financial assets measured at fair value** | | | | | | | | | |
| Investments | $ 5.1 | $ - | $ - | $ - | $ 5.1 | - | 5.1 | - | $ 5.1 |
| | $ 5.1 | $ - | $ - | $ - | $ 5.1 | | | | |
| **Financial assets not measured at fair value** | | | | | | | | | |
| Cash and cash equivalents | $ - | $ - | $ 6.0 | $ - | $ 6.0 | | | | |
| Trade and other receivables | - | - | 83.1 | - | 83.1 | | | | |
| | $ - | $ - | $ 89.1 | $ - | $ 89.1 | | | | |
| **Financial liabilities measured at fair value** | | | | | | | | | |
| Foreign currency forward contracts | $ - | $ 0.6 | $ - | $ - | $ 0.6 | - | 0.6 | - | $ 0.6 |
| | $ - | $ 0.6 | $ - | $ - | $ 0.6 | | | | |
| **Financial liabilities not measured at fair value** | | | | | | | | | |
| Accounts payable and accrued liabilities | $ - | $ - | $ - | $ 98.3 | $ 98.3 | | | | |
| Long-term debt (Note 9) | - | - | - | 73.1 | 73.1 | | | | |
| | $ - | $ - | $ - | $ 171.4 | $ 171.4 | | | | |
| **December 31, 2014** | | | | | | | | | |
| **Financial assets measured at fair value** | | | | | | | | | |
| Investments | $ 5.0 | $ - | $ - | $ - | $ 5.0 | - | 5.0 | - | $ 5.0 |
| | $ 5.0 | $ - | $ - | $ - | $ 5.0 | | | | |
| **Financial assets not measured at fair value** | | | | | | | | | |
| Cash and cash equivalents | $ - | $ - | $ 1.8 | $ - | $ 1.8 | | | | |
| Trade and other receivables | - | - | 65.6 | - | 65.6 | | | | |
| | $ - | $ - | $ 67.4 | $ - | $ 67.4 | | | | |
| **Financial liabilities measured at fair value** | | | | | | | | | |
| Foreign currency forward contracts | $ - | $ 0.3 | $ - | $ - | $ 0.3 | - | 0.3 | - | $ 0.3 |
| | $ - | $ 0.3 | $ - | $ - | $ 0.3 | | | | |
| **Financial liabilities not measured at fair value** | | | | | | | | | |
| Accounts payable and accrued liabilities | $ - | $ - | $ - | $ 76.3 | $ 76.3 | | | | |
| Long-term debt (Note 9) | - | - | - | 73.0 | 73.0 | | | | |
| | $ - | $ - | $ - | $ 149.3 | $ 149.3 | | | | |

*(Tabular amounts expressed in millions of Canadian dollars except number of shares and per share amounts)*

## 15. Financial instruments – fair values (continued)

As at March 31, 2015, the Company had outstanding obligations to sell an aggregate Japanese Yen ("JPY") 600 million at an average rate of JPY 97.00 per CAD with maturities through May 21, 2015, and an aggregate US$18.0 million at an average rate of CAD$1.2441 per US with maturities through May 14, 2015. All foreign currency gains or losses related to currency forward contracts to March 31, 2015 have been recognized in revenue for the period and the fair value of these instruments at March 31, 2015 was a net liability of $0.6 million, which is included in accounts payable and accrued liabilities on the statement of financial position (December 31, 2014: net liability of $0.3 million). A net loss of $4.3 million was recognized on contracts which were settled in the three months ended March 31, 2015 (2014: net loss of $1.1 million), which was included in revenue for the period.

## 16. Discontinued operations

In March 2006, the Company closed its Squamish pulp mill located on 212 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 have been expensed as incurred.

In January 2013, Western announced that it had entered into a conditional agreement for the sale of its former Squamish pulp mill site. Closing was subject to certain conditions and Western was responsible for the satisfactory remediation of the property to applicable environmental standards prior to closing the sale. During 2013, both parties agreed to a specific remediation plan, and a deposit of $5.5 million was placed in trust by the purchaser. In 2014, the Company completed its remediation plan in accordance with the terms of the agreement.

On February 6, 2015, the Company completed the sale of its former Squamish pulp mill site for proceeds of $21.8 million and recognized a gain on disposition of $5.4 million during the three months ended March 31, 2015.

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

| | Three months ended March 31, | |
|---|---|---|
| | 2015 | 2014 |
| Net income from discontinued operations | $ 9.1 | $ - |
| Cash provided by discontinued operations | $ 20.9 | $ - |

| | March 31, 2015 | December 31, 2014 |
|---|---|---|
| Assets of discontinued operations, excluding land | $ - | $ 2.8 |
| Liabilities of discontinued operations | $ - | $ 4.8 |

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