Western Forest Products Inc.

2012 Third Quarter Report

November 7, 2012

To our Shareholders,

A US recovery is now underway with new housing starts accelerating. Japan is showing signs of improvement and China remains a key market. We continue to position Western to take full advantage of these market improvements. Our margin focus, repositioned cost structure, and flexibility allowed us to post our twelfth consecutive quarter of positive EBITDA.

British Columbia's driest summer in over 100 years impacted log supply. Despite this, our sawmill productivity continued to climb, and our timberlands performed well in delivering volume even with operating days being reduced significantly. Demand for our lumber products increased, our lumber order file emerged from the quarter strong, and our liquidity and debt position is the best it has been since the company's inception.

Q3 2012 financial highlights are as follows:

- EBITDA for the quarter was $8.4 million, our twelfth consecutive quarter of positive EBITDA
- Net debt decreased to $19.7 million, a new record low for Western
- Liquidity continues to increase and is now at $178.0 million
- Sales revenue remained strong at $219.4 million

The quarter resulted in several achievements including:

- Lumber revenue increased 4% compared to the same quarter last year
- Manufacturing mill productivity per shift for the quarter improved 13% over the third quarter 2011
- Lumber shipments into North America increased to 60% of our sales from 48% a year ago

Western's ability to be responsive to shifts in lumber markets allowed us to divert volume into an improving North American lumber market and maintain strong sales revenues. During the third quarter, the lumber markets in North America, driven by the US, steadily improved. Rising building permits for new construction and housing starts provided improved market opportunities, and are pointing to an accelerated recovery in the US. We took advantage of this trend and redirected a higher percentage of our lumber production into the North American market. The Japanese market continues to show signs of improvement, from both a price and volume perspective, and China's demographics indicate a market that will have long-term strength. Our ability to be flexible and respond to market demand is a competitive advantage.

Severely dry weather conditions impacted operating days and supply. Due to the weather, we operated fewer days in our timberlands and many days we were forced to operate on a reduced workday. Log harvest volumes were 17% lower than the same quarter last year and 22% lower than the previous quarter this year. The reduced harvest resulted in a 20% reduction in log revenues and fibre supply to our mills was insufficient to allow us to satisfy market demand for our products. We expect weather conditions to continue to impact supply into the fourth quarter. We will be concentrating on building our log inventory in preparation for 2013 and maintaining our focus on getting maximum margin from every log.

Log markets didn't see the same improvements in the quarter but we are beginning to see signs of a stronger market going forward. During the quarter, we experienced weaker demand in our export markets for our logs, specifically Japan, Korea, and China which led to both lower volumes and prices. Our expectation is that shipments will return to more normal levels in 2013. In addition, due to lower prices for market pulp, our sales of pulp logs and chips to our coastal pulp mill customers were similarly impacted and we expect little improvement in the near term. However, as the US lumber markets continue to strengthen over the coming quarters, we expect the market for logs to tighten with increasing operating rates from mills along the coast of British Columbia and the Pacific Northwest. We have made organizational changes designed to enhance our position in log purchasing and trading to maximize margin in domestic and overseas log markets.

Western's focus on margin and strategic positioning produced continued positive results. Net debt continues to decline to its lowest level ever at $20 million - a significant improvement from the Company's debt position in 2008 at $233 million. Liquidity remains very strong at $178 million. Our manufacturing division has shown marked improvement in throughput in our sawmills and we have made gains in our transportation and procurement costs. We continue to seek opportunities and ideas through management collaboration and by fostering a culture of continuous improvement, hands on management, and margin focus.

A part of our strategic plan is investing in our mills in preparation for recovery in our markets. The $38 million upgrade of our Saltair sawmill is on time and on budget with $24 million committed and contractors selected. The project team is preparing the site for arrival of equipment and installation of the stacker over our Christmas shutdown. This $24 million phase will be completed at the end of the second quarter in the New Year. Our $6.7 million dollar investment in technology, the automated lumber grading equipment in our Alberni Pacific Sawmill, is expected to be complete at the end of the first quarter in 2013. These improvements will ensure our continued competitiveness in global lumber markets. We will keep you posted on our progress.

We are developing our management team to complement our margin focused business. This quarter we were pleased to announce the appointment of **Bruce St. John** as Vice President Lumber Sales and Marketing and **Tony Peiffer** as General Manager, Log Marketing.

Bruce has over 25 years of BC coastal lumber sales experience, and was most recently our General Manager of Whitewood Sales and Marketing. His primary focus will be bringing together our sales, manufacturing and timberlands groups to further refine our product line offerings to drive improved margin.

Tony also brings over 25 years of experience from the perspective of Coastal log marketing. Our margin focus necessitates expertise like Tony's to look at each block we harvest or purchase to ensure we are maximizing margin. Tony has a proven track record of delivering results in this area.

Our safety results continue to trend in a positive direction. We are committed to providing the systems, education, support and leadership necessary to deliver a zero incident work place for all of our employees. We demonstrate our commitment by leading the industry in key training initiatives such as danger tree assessment and we are proud to have launched new faller training and basic logger training programs this fall. We remain proactively focused on our contract operations as it is clear that improvement is needed here. Our goal is to ensure all workers operate in a "culture" of safety. This is the fundamental shift that will take improved safety results to the next level.

We expect to benefit materially from the recovery taking hold in the US housing industry and as we do so, we will continue to effectively manage factors within our control, and implement our strategic plan which is resulting in a strong financial position, short and long-term, with improved safety results. We would like to commend all of our employees for their continued focus on safety and margin and look forward to improved market and weather conditions in the last quarter of 2012.

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 and nine months ended September 30, 2012 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 audited annual consolidated financial statements and attached notes thereto, and management's discussion and analysis ("MD&A") for the year ended December 31, 2011 (the "2011 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 unaudited condensed consolidated interim financial statements for the three and nine months ended September 30, 2012 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 EBITDA[1]. EBITDA is defined as operating income prior to operating restructuring items and other expenses, plus amortization of property, plant, equipment, and intangible assets, impairment adjustments, and changes in fair value of 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, 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 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 International Financial Reporting Standards ("IFRSs") 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. EBITDA is not a measure of financial performance under IFRSs, and should not be considered as an alternative to measures of performance under IFRSs. 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. A reconciliation between the Company's net income as reported in accordance with IFRSs and EBITDA is included in Appendix A to this report.

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 this 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 November 7, 2012. 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.

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

Summary of Selected Quarterly Results[1]

(millions of dollars except per share amount)	Three months ended September 30 2012	Three months ended September 30 2011 Restated[(2)]	Nine months ended September 30 2012	Nine months ended September 30 2011 Restated[(2)]
Revenue	$ 219.4	$ 233.5	$ 694.2	$ 633.0
EBITDA	8.4	15.8	36.4	50.0
EBITDA as % of revenue	3.8%	6.8%	5.2%	7.9%
Operating income prior to restructuring items and other expenses	2.6	9.2	16.4	30.0
Net income from continuing operations	2.3	5.6	15.4	21.3
Net income for the period	2.0	5.3	14.5	20.5
Basic and diluted earnings per share (in dollars)	$ -	$ 0.01	$ 0.03	$ 0.04

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

(2) Restated to reflect accounting policy change as described on Page 9.

Overview

Third quarter 2012

During the third quarter, the lumber markets in North America continued to improve. Rising building permits for new construction and accelerating housing starts are now pointing to a recovery in the US housing industry. This is providing the opportunity for the Company to redirect some of its lumber production into North American markets to take advantage of an improving demand for its lumber products. Total revenue for the third quarter of 2012 was $219.4 million, a decline of $14.1 million from the third quarter of 2011. While our lumber revenue increased in the current quarter, revenues from both log and by-product sales reduced significantly, leading to the overall decline. Our results for the third quarter of 2012 were negatively impacted by log harvest restrictions related to higher than normal fire hazards in our timberlands operations, and reduced prices for pulp logs and by-products. As a result, our timberlands operations worked fewer days, and had restricted activities for certain periods of time. Overall log harvest production in the third quarter was 285,000m^3 (17%) lower than the third quarter of 2011, and 397,000m^3 (22%) less than the second quarter of 2012. The reduced harvest volume led to a 19% reduction in log sales volumes and an increase in logging costs per unit, compared to the same quarter last year.

The third quarter EBITDA result of $8.4 million is a decline from the $15.8 million figure reported in the third quarter a year ago. This decline is primarily the result of lower selling prices for our pulp and export logs, and a 19% reduction in the volume of logs sold compared to the third quarter of 2011. Unit log costs in the current quarter were also higher than the third quarter of 2011, driven by a combination of lower productivity and higher than anticipated repair and maintenance costs. Despite our log supply challenges, our manufacturing operations saw both production and productivity increases from the same quarter a year ago.

EBITDA for the three months ended September 30, 2011 was restated to $15.8 million, a decrease of $2.3 million, due to the adoption of a new inventory accounting policy on January 1, 2012. The annual impact of the policy change on our 2011 EBITDA results amounted to a decrease of $0.2 million.

Net income for the third quarter of 2012 was $2.0 million, a decrease of $3.3 million from the net income of $5.3 million a year earlier, and a decrease of $8.6 million from the net income in the previous quarter. The decrease in net income in the third quarter of 2012 compared to the same quarter a year ago is principally due to the reduced EBITDA of $7.4 million. This was partially offset by the inclusion of other non-operating gains this quarter of $1.1 million, compared to expenses of $1.9 million in the third quarter of 2011, a favourable fair value adjustment to the biological assets and slightly lower finance costs compared to the third quarter of last year.

Year to date, September 30, 2012

Net income for the first nine months of 2012 was $14.5 million, which compares to net income in the first nine months of 2011 of $20.5 million. EBITDA of $36.4 million for the nine months to September 30, 2012 is $13.6

million less than for the first nine months of 2011. Partially offsetting this decrease in EBITDA is an increase in other income of $6.2 million, mainly as a result of gains on property sales in the current period, and lower finance costs in the nine months ended September 30, 2012.

Our liquidity position at September 30, 2012 increased to $178.0 million from $175.5 million at the end of the previous quarter, and from $112.1 million at December 31, 2011.

Operating Results

Revenues

	Three months ended September 30		Nine months ended September 30	
(millions of dollars)	2012	2011	2012	2011
Lumber	$ 147.3	$ 141.2	$ 468.3	$ 413.7
Logs	58.5	77.3	183.4	171.4
By-products	13.6	15.0	42.5	47.9
Total revenues	$ 219.4	$ 233.5	$ 694.2	$ 633.0

Third quarter 2012

Lumber revenue for the third quarter of 2012 increased by 4% compared to the third quarter of 2011, primarily due to higher shipment volumes. Lumber shipment volumes increased by 4% to 218 million board feet in the third quarter of 2012 from 209 million board feet in the third quarter of 2011. Stronger markets in North America provided the opportunity to ship 60% of our lumber into the North American markets and away from China and Japan where weaker economic activity had led to a modest decline in demand. We believe this flexibility is a competitive advantage for Western that will add considerable value over the short and long term.

In the third quarter of 2012, our overall realized average lumber price of $676 per thousand board feet was approximately the same as that in the third quarter of 2011. In general, lumber prices did not change significantly over the two quarters. Our lumber sales mix in the current quarter changed marginally with approximately 3% more hemlock and western red cedar sales and 6% less douglas fir sales this quarter, compared to the third quarter of 2011.

Log revenue in the third quarter of 2012 was $58.5 million, a decrease of 24% compared to the same quarter last year. The decrease is due to a 19% reduction in the volume of logs sold, combined with the average log prices realized in the third quarter of 2012 being 4%, or $3 per cubic metre, lower than a year ago. Weather related curtailments in the third quarter of 2012 in our timberland operations led to production volumes that were 83% of third quarter 2011 levels. Export log prices decreased in 2012 as a result of lower demand in China and Japan. Domestic pulplog prices were 16% lower in the current quarter compared to the third quarter 2011 due to decreased market pulp prices.

By-product revenues decreased by $1.4 million, or 9%, in the current quarter compared to the third quarter of 2011. While chip volumes sold in this quarter were 10% higher than the third quarter last year, prices received for the chips were on average 20% lower this quarter, which more than offset the impact of the favourable volume increase. Prices realized for our chips sold under fibre agreements with certain of our customers are based on a chip pricing formula, which is a function of pulp prices and the mix of chips sold. Pulp prices were significantly lower in the current quarter compared to the same quarter in 2011, with a drop in demand for NBSK pulp from China being the primary cause for this. This price reduction resulted in the lower chip prices.

EBITDA

EBITDA of $8.4 million for the third quarter of 2012 compares to $15.8 million for the same quarter last year, and to $18.7 million in the second quarter of 2012. The decline in EBITDA for the current quarter of 2012 compared to the third quarter of 2011 is mainly the result of lower log harvesting levels, higher log costs, lower log sales prices and volumes, and lower by-product prices.

As already mentioned, a prolonged spell of particularly hot and dry weather in the third quarter severely impacted our ability to harvest logs. Current quarter harvest levels were 17% lower than in the third quarter of 2011, which has led to higher unit operating costs this year. Spending on repair and maintenance costs on mobile equipment was also higher in the current quarter. In addition to higher operating costs, our timberlands operations received less revenue from other operating activities, such as market logging and our joint ventures with First Nations. In conjunction with these higher costs, log sale margins were further compressed by the lower log sales prices as described above, and lower shipment volumes compared to the same period last year.

Despite operating less shifts, our primary sawmill lumber production was 7% higher in the third quarter of 2012 compared to the third quarter of 2011, reflecting a higher productivity level in the current quarter, measured on a volume per shift basis. The Ladysmith, Somass and Cowichan Bay mills lost some shifts due to log supply shortages, and the Chemainus mill took maintenance downtime. In addition, conversion costs of lumber produced by our primary sawmills in the third quarter of 2012 decreased by 2% from the same period a year ago. These productivity improvements and reduced conversion costs reflect the ongoing initiatives undertaken as part of the company-wide margin improvement program initiated in 2011.

Our operating results for the third quarter of 2012 were positively impacted by a weakening of the average value of the Canadian dollar relative to both the US dollar and Japanese Yen compared to the third quarter of 2011, by 2% and 1%, respectively. This increased our Canadian dollar proceeds received on US dollar denominated sales (a high percentage of our lumber sales are denominated in US dollars, including those to China), and also on Yen denominated sales.

Total freight costs were $19.0 million in the third quarter of 2012, which compares to the third quarter of 2011 costs of $23.8 million. The primary reason for the reduction in freight costs was a change in the mix of regions to which lumber sales were made, with a swing from 60% to domestic markets and 40% to export markets in the third quarter of 2012 compared to 48% and 52%, respectively, in the third quarter 2011. The other significant factor contributing to the lower freight costs this quarter was the decline in volumes of log exports compared to the third quarter of 2011.

Selling and administration costs increased by $0.5 million to $6.9 million in the current quarter compared to $6.4 million in the same quarter of 2011, mainly due to increased salary costs and higher investments in information systems technology, primarily associated with projects to enhance the quality of our management and sales information.

Year to date, September 30, 2012

Total revenues for the first nine months of 2012 were $694.2 million, an increase of 10% over the revenues for the same period in 2011. The increase is the result of higher demand for all lumber and logs with volume increases for the current nine month period for lumber and logs being 12% and 11%, respectively. Lower pulplog and by-product pricing in the nine months to September 31, 2012 compared to the same period in 2011 has partially offset the impact of the volume increases.

EBITDA for the first nine months of 2012 was $36.4 million compared to $50.0 million earned in the first nine months of 2011. EBITDA margins fell from 7.9% to 5.2%. The primary reason for the contraction of the margins has been the decreased log margins due to reduced selling prices of export and most domestic logs, along with increases in our log costs over the respective periods. The cost of our logs sold in the first nine months of 2012 was higher than 2011, as we drew down inventories that carried higher costs incurred in the fourth quarter of 2011 and experienced higher operating costs in the third quarter of 2012.

Non-operating income and costs

Finance costs decreased from $1.5 million in the third quarter of 2011 to $1.1 million in the current quarter. This decrease is primarily attributable to a reduction in our outstanding debt amount over the respective periods, combined with a lower interest rate in the current quarter compared to 2011. For similar reasons, finance costs for the first nine months of 2012 of $4.0 million were lower than the $5.2 million incurred for the first nine months a year ago.

Other income of $1.1 million for the third quarter of 2012 compares to a net expense of $1.9 million in the third quarter of 2011. The current quarter income mainly comprises proceeds received from the Province of British Columbia as final compensation resulting from the creation of new protective areas in our Haida Gwaii and Central Coast operating areas. The expense of $1.9 million in the comparable quarter in 2011 related to impairment losses taken on intangible and other assets resulting from the sale of TFL 60.

Financial Position and Liquidity

(millions of dollars except where noted)	Three months ended September 30 2012	Three months ended September 30 2011	Nine months ended September 30 2012	Nine months ended September 30 2011
Cash provided by (used in) operating activities	$ 18.8	$ (1.2)	$ 46.6	$ 24.3
Cash provided by (used in) investing activities	(7.2)	(3.1)	(9.7)	18.4
Cash provided by (used in) financing activities	(16.0)	3.7	(27.0)	(43.6)
Cash used to construct capitalized logging roads	(2.7)	(3.6)	(7.8)	(6.7)
Cash used to acquire property, plant and equipment	(5.8)	(2.8)	(13.6)	(6.2)

	September 30, 2012	December 31 2011
Total liquidity[1]	$ 178.0	$ 112.1
Net debt [2]	19.7	52.1
Financial ratios:		
Current assets to current liabilities	2.30	2.30
Net debt to capitalization[3]	0.05	0.13

(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 third quarter of 2012 amounted to $18.8 million compared to cash used of $1.2 million in the same period last year. The positive swing of $20.0 million is largely driven by the relative movements on investment in working capital in the two quarters. Most of the improvement in the cash generated from working capital arises from the relative levels of accounts receivable and inventories over the respective periods. In the third quarter of 2012, receivables were lower than normal based on timing of receipts in September. In the case of inventories the balance was unusually low at the end of the third quarter of 2012, due to increased downtime because of fire restrictions.

Cash used for additions to property, plant and equipment in the third quarter of 2012 was $8.5 million compared to $6.4 million in the third quarter of 2011. In the current quarter, additions comprised $2.7 million of additions to logging roads and bridges, $3.3 million on maintenance capital (primarily mobile equipment replacements/upgrades), and $2.5 million was invested in strategic capital projects. The strategic spend mainly related to the Saltair sawmill stacker, sorter and trimline rebuild projects.

During the third quarter of 2012, the Company paid down $15.0 million on the revolving term loan facility from cash received from asset sales and surplus cash generated from operations.

For the first nine months of 2012, the Company received net proceeds of $11.7 million from the sale of assets, of which $10.2 million related to the sale of TFL 60. In the first nine months of 2012, the Company repaid $8.9 million on its revolving credit facility out of cash generated from operations, in addition to repayments of $14.1 million on the revolving term loan.

In the first nine months of 2011, we received proceeds of $31.3 million from the sale of assets, the most significant being the sale to TimberWest Forest Corp. of 7,678 hectares of land located in the southern part of Vancouver Island for gross proceeds of $21.9 million. During the first nine months of 2011, the Company paid down its non-revolving term loan by $47.1 million as a result of cash generated from the sales of non-core assets, $5.2 million cash received as reimbursement by the Province of British Columbia for costs incurred by Western with respect to the Forestry Revitalization Plan timber take-back areas, and the balance from cash generated from operations.

At September 30, 2012, Western's total liquidity increased to $178.0 million from $112.1 million at the end of 2011 and from $116.0 million at September 30, 2011. At September 30, 2012, liquidity was comprised of cash of $24.3 million and availability under the revolving credit facility and revolving term loan of $88.7 million and $65.0 million, respectively. The increase in liquidity compared to September 30, 2011 was primarily due to the additional $35.0 million available under the recently revised financing agreement, and the cash received from the sale of TFL 60. In addition, an increase in borrowing base assets, specifically, eligible accounts receivable and inventory, resulted in an increase in availability under the revolving credit facility.

Adjustment of Second Quarter 2012 Net Income

Subsequent to filing the interim financial statements for the three and six months ended June 30, 2012, management discovered an error relating to the second quarter net income. Management has adjusted net income for the second quarter as it facilitates an understanding of the respective results for the second and third quarters of 2012. The adjustment is reflected in the Summary of Selected Results for the Last Eight Quarters – Appendix A (see footnote 3), and resulted in an increase to the unrealized loss related to currency forward contracts and recognized in revenues, and a decrease to net income of $1.7 million from that previously recorded for the three and six months ended June 30, 2012.

Accounting Policies

(a) Change in accounting policy

Inventories

On January 1, 2012, the Company changed its accounting policy with respect to the costing of log inventories from the distributed cost method to the average cost of production method. Under the new policy, the costs of logs produced will carry an average cost of production based on the operation where the logs are produced, determined by actual log production costs divided by production volumes. This compares to the former policy which allocated costs based on the estimated fair value of the logs produced. Management believes that this change in accounting policy provides more relevant information about the financial performance of the Company to the users of the financial statements, as it aligns the costing methods of the Company's log and lumber inventories, is more consistent with industry accounting practices and also results in a more conservative carrying value relative to the previous method used.

This change in accounting policy was applied retrospectively with prior periods being restated accordingly. The change resulted in a $10.1 million reduction to the carrying value of inventory and a corresponding increase to the deficit as at December 31, 2011. For the quarter ended September 30, 2011, the policy change resulted in an increase to cost of goods sold and a decrease to earnings of $2.3 million (decrease to cost of goods sold and increase to earnings of $1.8 million for the nine months to September 30, 2012).

(b) Adoption of new accounting policies

A number of new International Accounting Standards, and amendments to standards and interpretations, are not yet effective, and have not yet been applied in preparing these interim financial statements. None of these are expected to have a significant effect on the consolidated financial statements of the Company, except for IFRS 9, *Financial Instruments* which becomes mandatory for the Company's 2015 consolidated financial statements and is expected to impact the classification and measurement of financial assets. IFRS 9 replaces the guidance in IAS 39, *Financial Instruments: Recognition and Measurement*, on the classification and measurement of financial assets. IAS 9 eliminates the existing IAS 39 categories of held to maturity, available-for-sale and loans and receivables. Financial assets will be classified into one of two categories on initial recognition: financial assets measured at amortized cost or financial assets measured at fair value. The extent of the impact has not been determined.

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, 2011. 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 controls over financial reporting during the third quarter of 2012.

Outlook and Strategy

Recent positive data relating to the US housing industry, combined with housing affordability rates at near record high levels, supports our view that a recovery is underway and accelerating in the US. Continued improvement in home construction activity is expected to directly and indirectly increase demand for all our lumber products including Western Red Cedar for external applications; value added Niche products for internal appearance grades including exposed beams and trim; and, Commodity products for structural applications.

While we normally anticipate some seasonal weakness in the fourth quarter for our high value Western Red Cedar, as a result of the reduced harvest levels in the most recent quarter, we are now expecting cedar prices to remain firm through the year end and into 2013. Our fourth quarter product focus will be on industrial products for the BC remanufacturing community. Our operating focus for the fourth quarter is to manage our cedar inventories, in preparation for the peak US selling season in the first half of 2013.

The Japanese market has shown signs of improvement after a slow summer. In response to an increase in inquiries for Hemlock Squares we are planning to increase production at our mills. The increase in demand has allowed us to increase prices in October and November. We are also seeing some increased demand for Douglas Fir as US producers have reduced their Japanese exports to service the US domestic market. Demand for custom cut volumes of Yellow Cedar for the fourth quarter are forecast to be stronger than the third quarter. We expect to have to adjust production and shipping schedules in the fourth quarter to lessen the impact of any weather related delays in our logging program.

In our Niche segment, the North American market for appearance grade products remains soft and year over year volumes are flat. We do not foresee a significant change in North American sales in the fourth quarter, as our customer base indicates they have sufficient inventories. We will continue to reposition some of our shop and better grade production to China. We are anticipating a slight improvement in European sales, where there is increasing interest in purchasing, albeit at lower price levels.

Commodity lumber volumes in the third quarter were down 5% from second quarter levels, primarily due to log supply issues, which are expected to persist into the fourth quarter. The shortages in supply, along with our newly developed local sales channels, have allowed us to increase pricing through to the end of the third quarter and into the fourth quarter. The traditional seasonal slowdown in housing demand in the US is starting to impact benchmark kiln-dried SPF pricing, which may eventually put price pressure on our commodity products. However, any price reductions are not expected to affect us until late in the fourth quarter, given our strong order file position. Demand for mat stock and timbers for use in the oil exploration industry have had a slow start to the fall season, due to an exceptionally dry summer and early fall.

With respect to logs, demand is expected to increase due to the coast-wide weather related production curtailments. Export log prices in China and Korea have stabilized and we expect price appreciation through the fourth quarter as customers replenish their depleted inventories. Pulplog demand is expected to remain flat heading into the fourth quarter as the price for pulp remains under pressure.

We are positioning ourselves for the coming recovery in the housing markets and are implementing a comprehensive strategic capital plan to ensure our continued competitiveness in the global lumber markets. Our balance sheet is strong, and we expect that the strategic capital program will be funded by cash generated from operations. These capital projects are expected to further enhance our margins through improved efficiencies and product grades. The first two projects are underway.

Our first project is the $38 million upgrade of our Saltair sawmill. The project is on time and on budget with $24 million committed and contractors selected. Our project team is preparing the site for arrival of equipment and installation of the stacker over the Christmas shutdown. This $24 million phase includes a full upgrade to the edgers, trimmer, sorter and stacker for the mill and will be complete at the end of the second quarter of 2013. Our second project, the automated lumber grading project being initiated at our Alberni Pacific sawmill is also expected to be complete in the second quarter of 2013.

Complementing our strategic capital investment program, we continue to work on the non-capital margin improvement program. This program is targeted to deliver an additional $25 million in margin enhancements over the next three years through a variety of cost reduction and productivity initiatives across the organization. We remain on schedule to achieve approximately one third of these benefits by the end of 2012, with the majority relating to manufacturing throughput and logistics enhancements.

Risks and Uncertainties

The business of the Company is subject to a number of risks and uncertainties, including those described in the 2011 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 effect on our operations and financial condition and cash flows and, accordingly, should be carefully considered in evaluating Western's business.

Outstanding Share Data

As of November 7, 2012, there were 129,105,623 Common Shares and 338,945,860 Non-Voting Shares issued and outstanding. Brookfield Special Situations Management Limited ("BSSML") controls and directs 48.82% 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 an independent committee of the Board of Directors has determined that to do so would not have a material adverse effect on the Company's business, financial condition or business prospects at such time.

Western has reserved 9,520,000 Common Shares for issuance upon the exercise of options granted under the incentive stock option plan. On February 22, 2012 and July 31, 2012, 1,800,000 options and 2,900,000 options, respectively, were granted under the plan. As of November 7, 2012, 9,516,795 options were outstanding under the Company's incentive stock option plan.

Related Parties

By virtue of the Brookfield Asset Management Inc. ("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, the provision of a foreign exchange facility, and the services of the Chief Executive Officer, all in the normal course and at market rates or at cost. During the third quarter of 2012, the Company paid entities related to BAM $5.5 million ($10.6 million year-to-date), and received income from related entities of $1.4 million ($4.7 million year-to-date) in connection with these arrangements.

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	Lee Doney Vice-Chairman

Vancouver, BC,

November 7, 2012

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)	2012 3rd	2012 2nd [3]	2012 1st	2011 4th	2011 3rd	2011 2nd	2011 1st	2010 4th
Average Exchange Rate – Cdn $ to purchase one US $	0.996	1.010	1.001	1.023	0.980	0.968	0.986	1.013
Revenue								
Lumber	147.3	163.8	157.2	147.4	141.2	143.5	129.0	118.1
Logs	58.5	73.0	51.9	60.2	77.3	57.8	36.3	38.8
By-products	13.6	14.6	14.3	13.1	15.0	17.4	15.5	15.7
Total revenue	219.4	251.4	223.4	220.7	233.5	218.7	180.8	172.6
Lumber								
Shipments – millions of board feet	218	234	220	209	209	210	183	168
Price – per thousand board feet	676	700	716	705	676	684	705	703
Logs								
Shipments – thousands of cubic metres	876	1,020	699	853	1,078	755	504	646
Price – per cubic metre[1]	65	70	72	69	68	72	68	60
Selling and administration	6.9	7.4	7.8	6.9	6.4	6.7	6.6	7.6
EBITDA[2]	8.4	18.7	9.3	11.6	15.8	21.2	13.0	2.8
Amortization	(6.2)	(6.9)	(6.8)	(5.7)	(6.0)	(6.7)	(5.6)	(5.2)
Changes in fair value of biological assets	0.4	(0.4)	(0.1)	(0.9)	(0.6)	(0.5)	(0.6)	(0.8)
Reversal of impairment	-	-	-	-	-	-	-	18.5
Operating restructuring items	(0.2)	(0.4)	-	0.2	(0.3)	(0.3)	(0.3)	(0.1)
Finance costs	(1.1)	(1.6)	(1.3)	(1.4)	(1.5)	(1.8)	(1.9)	(2.8)
Other income (expenses)	1.1	1.6	1.0	(0.3)	(1.9)	(0.1)	(0.5)	6.3
Income taxes recovery (expense)	(0.1)	-	-	0.1	0.1	(0.2)	-	0.6
Net income from continuing operations	2.3	11.0	2.1	3.6	5.6	11.6	4.1	19.3
Net loss from discontinued operations	(0.3)	(0.4)	(0.2)	(0.3)	(0.3)	(0.2)	(0.3)	(0.3)
Net income	2.0	10.6	1.9	3.3	5.3	11.4	3.8	19.0
EBITDA as % of revenues	3.8%	7.4%	4.2%	5.3%	6.8%	9.7%	7.2%	1.6%
Earnings per share:								
Net income, basic and diluted	-	0.02	-	0.01	0.01	0.02	0.01	0.04
Net income from continuing operations, basic and diluted	-	0.02	-	0.01	0.01	0.02	0.01	0.04

[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.

[2] EBITDA has been restated to reflect the accounting policy change as described on page 9 of the MD&A

[3] Revenue has been adjusted to reflect the accounting error as described on page 9 of the MD&A

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 North American 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.

The category of "Other income (expenses)" 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 second and third quarters of 2012, the third quarter of 2011 and the fourth quarter of 2010.

Western Forest Products Inc.

Unaudited Condensed Consolidated Interim Financial Statements

For the three and nine months ended September 30, 2012 and 2011

Western Forest Products Inc.

Condensed Consolidated Statements of Financial Position

(Expressed in millions of Canadian dollars) (unaudited)

	September 30, 2012	December 31, 2011 [Restated - Note 3(a)]
Assets		
Current assets:		
Cash and cash equivalents	$ 24.3	$ 15.3
Trade and other receivables	68.4	64.4
Inventory (Notes 3(a) and 7)	124.8	132.6
Prepaid expenses and other assets	6.0	6.5
	223.5	218.8
Non-current assets:		
Property, plant and equipment (Note 8)	193.5	190.3
Intangible assets (Note 8)	114.1	116.6
Biological assets (Note 9)	61.1	59.4
Assets classified as held for sale (Note 21)	-	11.5
Other assets	13.8	11.7
	$ 606.0	$ 608.3
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 77.2	$ 66.7
Revolving credit facility (Note 10)	-	8.9
Silviculture provision (Note 12)	13.7	13.3
Discontinued operations (Note 5)	6.3	6.2
	97.2	95.1
Non-current liabilities:		
Long-term debt (Note 11)	44.0	58.5
Silviculture provision (Note 12)	16.8	16.2
Liabilities classified as held for sale (Note 21)	-	1.4
Other liabilities (Note 13)	39.8	31.6
Deferred revenue	66.9	68.4
	264.7	271.2
Shareholders' equity:		
Share capital - voting shares (Note 15)	412.5	412.3
Share capital - non-voting shares (Note 15)	187.5	187.5
Contributed surplus	3.8	3.4
Revaluation reserve	23.9	23.9
Deficit (Note 3(a))	(286.4)	(290.0)
	341.3	337.1
	$ 606.0	$ 608.3

Commitments and Contingencies (Note 16)

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 (Loss)

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

	Three months ended September 30		Nine months ended September 30	
	2012	2011 [Restated - Note 3(a)]	2012	2011 [Restated - Note 3(a)]
Revenue	$ 219.4	$ 233.5	$ 694.2	$ 633.0
Cost and expenses:				
Cost of goods sold (Note 3(a))	189.9	192.4	583.4	509.3
Export tax	1.0	1.7	5.1	5.0
Freight	19.0	23.8	67.2	69.0
Selling and administration	6.9	6.4	22.1	19.7
	216.8	224.3	677.8	603.0
Operating income prior to restructuring items and other expenses	2.6	9.2	16.4	30.0
Operating restructuring items	(0.2)	(0.3)	(0.6)	(0.9)
Other income (expenses) (Note 18)	1.1	(1.9)	3.7	(2.5)
Operating income	3.5	7.0	19.5	26.6
Finance costs	(1.1)	(1.5)	(4.0)	(5.2)
Income before income taxes	2.4	5.5	15.5	21.4
Income tax expense	(0.1)	0.1	(0.1)	(0.1)
Net income from continuing operations	2.3	5.6	15.4	21.3
Net loss from discontinued operations (Note 5)	(0.3)	(0.3)	(0.9)	(0.8)
Net income for the period	2.0	5.3	14.5	20.5
Other comprehensive income (loss)				
Defined benefit plan actuarial losses	(3.8)	(14.7)	(10.9)	(16.3)
Total comprehensive income (loss) for the period	$ (1.8)	$ (9.4)	$ 3.6	$ 4.2
Net income per share (in dollars):				
Basic and diluted earnings per share	$ 0.00	$ 0.01	$ 0.03	$ 0.04
Basic and diluted earnings per share - continuing operations	$ 0.00	$ 0.01	$ 0.03	$ 0.04
Weighted average number of shares outstanding				
Basic	468,051	467,571	467,910	467,571
Diluted	476,696	474,013	475,438	473,646

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 September 30		Nine months ended September 30,	
	2012	2011 [Restated - Note 3(a)]	2012	2011 [Restated - Note 3(a)]
Cash provided by (used in):				
Operating activities:				
Net income from continuing operations	$ 2.3	$ 5.6	$ 15.4	$ 21.3
Items not involving cash:				
Amortization of property, plant and equipment (Note 8)	5.4	5.1	17.4	15.6
Amortization of intangible assets (Note 8)	0.8	0.9	2.5	2.7
(Gain) loss on disposal of assets	-	-	(3.2)	1.1
Change in fair value of biological assets (Note 9)	(0.4)	0.6	1.3	1.7
Finance costs	1.1	1.5	4.0	5.2
Other	(1.6)	0.9	(4.7)	0.9
	7.6	14.6	32.7	48.5
Changes in non-cash working capital items:				
Trade and other receivables	13.4	(3.8)	(5.3)	(24.0)
Inventory	2.1	(11.6)	7.8	(15.3)
Prepaid expenses and other assets	1.5	2.1	0.5	(1.9)
Silviculture provision	0.8	(0.1)	0.4	2.0
Accounts payable and accrued liabilities	(6.6)	(2.4)	10.5	15.0
	11.2	(15.8)	13.9	(24.2)
	18.8	(1.2)	46.6	24.3
Investing activities:				
Additions to property, plant and equipment	(8.5)	(6.4)	(21.4)	(12.9)
Proceeds on disposals of assets	1.3	3.3	11.7	31.3
	(7.2)	(3.1)	(9.7)	18.4
Financing activities:				
Changes in revolving credit facility	-	8.2	(8.9)	8.2
Interest paid	(1.0)	(1.2)	(3.2)	(4.6)
Repayment of long-term debt (Note 11)	(15.0)	(3.3)	(17.8)	(47.1)
Draw down of long-term debt	-	-	3.7	-
Refinancing fees	-	-	(1.0)	(0.1)
Proceeds from exercise of stock options	-	-	0.2	-
	(16.0)	3.7	(27.0)	(43.6)
Cash provided by (used in) continuing operations	(4.4)	(0.6)	9.9	(0.9)
Cash used in discontinued operations (Note 5)	(0.3)	(0.3)	(0.9)	(0.8)
Increase (decrease) in cash and cash equivalents	(4.7)	(0.9)	9.0	(1.7)
Cash and cash equivalents, beginning of period	29.0	4.3	15.3	5.1
Cash and cash equivalents, end of period	$ 24.3	$ 3.4	$ 24.3	$ 3.4

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, 2011, as previously reported	$ 599.8	$ 3.0	$ 23.9	$ (292.5)	$ 334.2
Change in accounting policy (Note 3(a))	-	-	-	(9.9)	(9.9)
Balance at January 1, 2011, as restated (Note 3(a))	599.8	3.0	23.9	(302.4)	324.3
Net income for the period	-	-	-	20.5	20.5
Other comprehensive income:					
Defined benefit plan actuarial losses recognized	-	-	-	(16.3)	(16.3)
Total comprehensive income for the period	-	-	-	4.2	4.2
Share-based payment transactions recognized in equity	-	0.3	-	-	0.3
Total transactions with owners, recorded directly in equity	-	0.3	-	-	0.3
Balance at September 30, 2011, as restated (Note 3(a))	$ 599.8	$ 3.3	$ 23.9	$ (298.2)	$ 328.8
Balance at January 1, 2012, as previously reported	$ 599.8	$ 3.4	$ 23.9	$ (279.9)	$ 347.2
Change in accounting policy (Note 3(a))	-	-	-	(10.1)	(10.1)
Balance at January 1, 2012, as restated (Note 3(a))	599.8	3.4	23.9	(290.0)	337.1
Net income for the period	-	-	-	14.5	14.5
Other comprehensive loss:					
Defined benefit plan actuarial losses recognized	-	-	-	(10.9)	(10.9)
Total comprehensive loss for the period	-	-	-	3.6	3.6
Share-based payment transactions recognized in equity	-	0.5	-	-	0.5
Exercise of stock options	0.2	(0.1)	-	-	0.1
Total transactions with owners, recorded directly in equity	0.2	0.4	-	-	0.6
Balance at September 30, 2012	$ 600.0	$ 3.8	$ 23.9	$ (286.4)	$ 341.3

See accompanying notes to these unaudited condensed consolidated interim financial statements

1. Reporting Entity

Western Forest Products Inc. ("Western" or the "Company") is a major 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. These unaudited condensed consolidated interim financial statements as at September 30, 2012 and for the three and nine months ended September 30, 2012 and 2011 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 30 countries worldwide. The Company is listed on the Toronto Stock Exchange, under the symbol WEF.

2. Basis of Presentation

(a) Statement of compliance

These unaudited condensed consolidated interim financial statements ("interim financial statements") are for the three and nine months ended September 30, 2012. They have been prepared in accordance with IAS 34, *Interim Financial Reporting,* and do not include all of the information required for full annual financial statements.

These interim financial statements were approved by the Board of Directors on November 7, 2012.

(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;
- Liabilities for cash-settled share-based payment transactions are measured at fair value at each reporting period. Equity-settled share-based payment transactions are measured at fair value at grant date;
- Long-term debt is initially recognized at fair value, then at amortized cost;
- Derivative financial instruments are measured at fair value; and
- The defined benefit pension 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) Use of estimates and judgements

The preparation of interim financial statements in accordance with IAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, and revenue and expenses. Actual results may differ from these estimates. 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.

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 consolidated financial statements as at and for the year ended December 31, 2011.

(d) Adjustment of second quarter 2012 net income

Subsequent to filing the interim financial statements for the three and six months ended June 30, 2012, management discovered an error relating to the second quarter net income. Management adjusted net income for the second quarter, as it facilitates an understanding of the respective results for the second and third quarters. The adjustment resulted in a $1.7 million increase to the unrealized loss related to currency forward contracts and recognized in revenue, and a decrease to net income of $1.7 million from that previously reported, for the three and six months ended June 30, 2012.

3. Significant Accounting Policies

Except as described below, the accounting policies applied by the Company in these interim financial statements are the same as those applied by the Company in its consolidated financial statements as at and for the year ended December 31, 2011.

(a) Changes in accounting policies

Inventories

On January 1, 2012, the Company changed its accounting policy with respect to the costing of log inventories from the distributed cost method to the average cost of production method. Under the new policy, the costs of logs produced carry an average cost of production based on the operation where the logs are produced, determined by actual log production costs divided by production volumes. This compares to the former policy which allocated costs based on the estimated fair value of the logs produced. Management believes that this change in accounting policy provides more relevant information about the financial performance of the Company to the users of the financial statements, as it aligns the costing methods of the Company's log and lumber inventories, and is more consistent with industry accounting practices and also results in a more conservative carrying value relative to the previous method used.

This change in accounting policy was applied retrospectively with prior periods being restated accordingly. The change resulted in a $10.1 million reduction to the carrying value of inventory and a corresponding increase to the deficit as at December 31, 2011 (December 31, 2010: $9.9 million). For the quarter ended September 30, 2011 the policy change resulted in an increase to cost of goods sold and a decrease to earnings of $2.3 million (decrease to cost of goods sold and increase to earnings of $1.8 million for the nine months ended September 30, 2011) from that previously reported.

(b) Adoption of new accounting policies

A number of new standards, and amendments to standards and interpretations, are not yet effective, and have not yet been applied in preparing these interim financial statements. None of these are expected to have a significant effect on the consolidated financial statements of the Company, except for IFRS 9, *Financial Instruments,* which becomes mandatory for the Company's 2015 consolidated financial statements and is expected to impact the classification and measurement of financial assets. The extent of the impact has not 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. 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 part 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:

(Tabular amounts expressed in millions of Canadian dollars)

	Three months ended September 30		Nine months ended September 30	
	2012	2011	2012	2011
Net loss from discontinued operations	$ (0.3)	$ (0.3)	$ (0.9)	$ (0.8)
Cash used in discontinued operations	$ (0.3)	$ (0.3)	$ (0.9)	$ (0.8)

	September 30, 2012	December 31, 2011
Assets of discontinued operations	$ 2.2	$ 2.3
Liabilities of discontinued operations	$ 6.3	$ 6.2

The assets of discontinued operations are included in “Other assets” on the statement of financial position.

6. Related Parties

Brookfield Special Situations Management Limited (“BSSML”) controls and directs 48.82% 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 and nine months ended September 30:

	Three months ended September 30		Nine months ended September 30	
	2012	2011	2012	2011
Costs incurred for:				
Log purchases	$ 4.2	$ 4.2	$ 7.2	$ 8.7
Other	1.3	1.2	3.4	3.4
	$ 5.5	$ 5.4	$ 10.6	$ 12.1
Income received for:				
Log sales	$ 1.4	$ 2.6	$ 4.7	$ 4.6
Other	-	-	-	2.4
	$ 1.4	$ 2.6	$ 4.7	$ 7.0

7. Inventory

The following table summarizes the value of inventory on hand:

	September 30, 2012	December 31, 2011 [Restated - Note 3(a)]
Logs	$ 78.5	$ 88.3
Lumber	46.7	46.9
Supplies and other inventories	10.7	11.3
Provision for write downs	(11.1)	(13.9)
Total value of inventories	$ 124.8	$ 132.6
Inventory carried at net realizable value	$ 37.0	$ 43.1

The inventory is pledged as security against the revolving credit line.

(Tabular amounts expressed in millions of Canadian dollars)

During the third quarter of 2012, $189.9 million (2011: $192.4 million) of inventory was charged to cost of sales which included a reduction to the provision for write-down to net realizable value of $0.4 million (2011: an increase of $1.0 million).

During the nine months ended September 30, 2012, $583.4 million (2011: $509.3 million) of inventory was charged to cost of sales which included a reduction to the provision for write-down to net realizable value of $2.8 million (2011: $2.3 million).

8. Property, Plant and Equipment and Intangible Assets

at December 31, 2011	Buildings & equipment	Logging roads	Land	Total property, plant and equipment	Intangible assets
Cost of capital assets at December 31, 2011	$ 128.2	$ 113.1	$ 110.7	$ 352.0	$ 172.7
Accumulated amortization and impairment at December 31, 2011	(80.2)	(81.5)	-	(161.7)	(56.1)
Net book value at December 31, 2011	48.0	31.6	110.7	190.3	116.6
at September 30, 2012					
Net book value at December 31, 2011	48.0	31.6	110.7	190.3	116.6
Additions	13.6	7.8	0.5	21.9	-
Disposals	(0.1)	(0.2)	(1.0)	(1.3)	-
Amortization	(8.0)	(9.4)	-	(17.4)	(2.5)
Net book value at September 30, 2012	$ 53.5	$ 29.8	$ 110.2	$ 193.5	$ 114.1

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

	September 30, 2012	December 31, 2011
Cost	$ 81.9	$ 81.6

9. Biological Assets

	Three months ended September 30		Nine months ended September 30	
	2012	2011	2012	2011
Carrying value at beginning of period	$ 60.7	$ 61.0	$ 59.4	$ 77.7
Acquisition of biological assets in the period	-	-	5.6	-
Disposition of biological assets in the period	-	-	(2.6)	(15.7)
Change in fair value less costs to sell	-	-	(1.2)	-
Change in fair value resulting from growth and pricing	0.5	0.6	1.2	1.5
Harvested timber transferred to inventory during the period	(0.1)	(1.3)	(1.3)	(3.2)
Carrying value at end of period	$ 61.1	$ 60.3	$ 61.1	$ 60.3

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, and the underlying land considered a component of property, plant and equipment, which the Company has elected to record at fair value at each reporting date (Note 8).

At September 30, 2012, standing timber comprised approximately 26,129 hectares (December 31, 2011: 25,484 hectares), which range from newly planted cut-blocks to old-growth forests. During the third quarter of 2012 the Company harvested and scaled approximately 28,150m^3 of logs from its private timberlands, which had a fair value less selling costs of $2.1 million at the date of harvest (three months ended September 30, 2011: 76,515m^3 and $5.5 million, respectively). During the nine months ended September 30, 2012, the Company harvested and scaled approximately 171,885m^3 of logs from its private timberlands, which had a fair value less selling costs of $12.8 million at the date of harvest (nine months ended September 30, 2011: 295,218m^3 and $20.8 million, respectively).

(Tabular amounts expressed in millions of Canadian dollars)

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 acquisition and disposition of biological assets in the first nine months of 2012 relates to an exchange with the Province of British Columbia (the “Province”) of a parcel of the Company’s private timberlands on Northern Vancouver Island for Crown timberlands in the same area. The disposition reflected in the first nine months of 2011 primarily related to the sale of properties to TimberWest Forest Corp.

10. Revolving Credit Facility

The Company’s revolving credit 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 0.5% (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 term loan. During the first quarter of 2012, $8.9 million was repaid on the facility and at September 30, 2012 the facility was unused (December 31, 2011: $8.9 million). At September 30, 2012, $88.7 million of the facility was available to the Company. The interest rate for the revolving credit facility was 3.50% at September 30, 2012 (December 31, 2011: 3.50%).

11. Long-Term Debt

On June 29, 2012, the Company completed the refinancing of its existing revolving term loan facility. Under the terms of the new arrangement, availability under the existing $75.0 million revolving term loan has been increased to $110.0 million. The revised facility has a maturity date of June 29, 2016. During the third quarter of 2012, the Company made a $15.0 million lump-sum repayment of the debt.

The loan bears interest at an index rate, determined as the higher of (i) the Canadian Prime rate, and (ii) the 30 day Banker’s Acceptance rate plus 1.35%, plus the applicable index rate margin which ranges from 1.75% to 3.25%, or at the Company’s election, the applicable Banker’s Acceptance rate, plus the applicable BA rate margin which ranges from 2.75% to 4.25%. The applicable margin is grid-based, determined quarterly, and based on a leverage ratio calculated as the ratio of total debt to EBITDA for the trailing twelve months ending on the date of determination. The interest rate for the revolving term loan was 4.75% at September 30, 2012 (December 31, 2011: 5.75%).

	September 30, 2012	December 31, 2011
Canadian dollar debt		
Revolving term loan	$ 45.0	$ 59.1
Less transaction costs	(1.0)	(0.6)
	$ 44.0	$ 58.5

The transaction costs at September 30, 2012 relate to the new financing arrangements in the second quarter. These costs are deferred and being amortized to finance costs over the term of the loan using the effective interest rate method. Deferred transaction costs associated with the previous facility have been fully expensed.

The Company was in compliance with its financial covenants at September 30, 2012.

(Tabular amounts expressed in millions of Canadian dollars)

12. 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 September 30		Nine months ended September 30	
	2012	2011	2012	2011
Silviculture provision, beginning of period	$ 30.6	$ 29.4	$ 30.9	$ 27.3
Silviculture provision charged	3.6	4.1	10.1	10.6
Silviculture work payments	(3.7)	(4.3)	(9.3)	(8.5)
Disposition of intangible assets	-	-	(1.4)	(0.4)
Unwind of discount	-	0.1	0.2	0.3
Silviculture provision, end of period	30.5	29.3	30.5	29.3
Less current portion	13.7	11.5	13.7	11.5
	$ 16.8	$ 17.8	$ 16.8	$ 17.8

13. Other Liabilities

	September 30, 2012	December 31, 2011
Employee post-retirement benefits obligation (Note 14)	$ 37.1	$ 28.8
Environmental accruals	1.5	1.5
Other	1.2	1.3
	$ 39.8	$ 31.6

14. Employee Post-Retirement Benefits

Employee post-retirement benefit expense for the defined benefit salaried pension, non-pension plans, and defined contribution pension plan are recognized in cost and expenses is as follows:

	Three months ended September 30		Nine months ended September 30	
	2012	2011	2012	2011
Current service costs	$ 0.1	$ 0.1	$ 0.3	$ 0.3
Interest costs	1.5	1.6	4.5	4.8
Expected return on plan assets	(1.4)	(1.6)	(4.2)	(4.8)
Cost of defined benefit plans	0.2	0.1	0.6	0.3
Cost of defined contribution plan	2.6	2.4	7.4	7.0
Total cost of employee post-retirement benefits	$ 2.8	$ 2.5	$ 8.0	$ 7.3

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

	September 30, 2012	December 31, 2011
Present value of funded obligations	$ (136.8)	$ (125.8)
Fair value of plan assets	99.7	97.0
Liability recognized in the balance sheet	$ (37.1)	$ (28.8)

The change in the liability recognized in the statement of financial position at September 30, 2012 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 in the third quarter of 2012 was a decrease of 0.9% from the rate used at December 31, 2011 of 5.0%, and the actual return on assets in the quarter was 2.9%.

(Tabular amounts expressed in millions of Canadian dollars)

15. 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 September 30, 2012	129,105,623	$412.5	338,945,860	$187.5
Balance at December 31, 2011	128,625,623	$412.3	338,945,860	$187.5

Brookfield Special Situations Management Limited controls and directs 48.82% 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 an independent committee of the Board of Directors has determined that to do so would not have a material adverse effect on the Company's business, financial condition or business prospects at such time.

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.

In the first quarter of 2012, the Company granted 1,800,000 options with a fair value of $1.0 million as determined by the Hull-White option pricing model using the assumptions of a weighted average exercise price of $0.95 per Common Share, risk free interest rates within a range of 1.48% to 2.05%, volatility rates of between 59.4% to 63.5% 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 average price basis. In the third quarter of 2012, the Company granted 2,900,000 options with a fair value of $1.9 million as determined by the Hull-White option pricing model using the assumptions of an exercise price of $0.96 per Common Share, risk free interest rates within a range of 1.27% to 1.68%, volatility rate of 57.0% and an expected life of between 6 and 10 years. These options are only exercisable when the share price exceeds $0.70 for 60 days on a volume weighted 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.

During the first quarter of 2012, 480,000 options were exercised, in the second quarter of 2012 990,000 options were forfeited, and in the third quarter of 2012, 155,000 options expired. At September 30, 2012, 9,516,795 options were outstanding under the Company's Option Plan with a weighted average exercise price of $0.86 per Common Share. During the three and nine month periods ended September 30, 2012 the Company recorded compensation expense of $0.3 and $0.5 million respectively (2011: $0.2 and $0.3 million, respectively).

The Company also 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 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. In the first quarter of 2012, designated executive officers were allotted 116,163 DSUs at a price of $0.99 per DSU and a further 25,202 DSUs were granted to a director at a weighted average price of $0.98 per DSU. During the second quarter of 2012, a director was granted 5,623 DSUs at a price of $0.87 per DSU. During the third quarter of 2012, a director was granted 5,403 DSUs at a price of $1.09 per DSU. The cumulative number of DSUs outstanding at September 30, 2012 was 975,622 (December 31, 2011: 823,231). During the three and nine month periods ended September 30, 2012, the Company recorded compensation expense for these DSUs of $0.3 million and $0.4 million, respectively (2011: compensation recovery of $0.1 million and expense of $nil, respectively), with a corresponding adjustment to accounts payable and accrued liabilities.

16. Commitments and Contingencies

(a) 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 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 had met all fibre commitments as at December 31, 2011 and based on chip and pulp log volumes supplied year-to-date, the Company anticipates satisfying annual fibre commitments for 2012.

(b) Lumber duties

On January 18, 2011 the United States ("US") initiated proceedings against Canada with the London Court of Arbitration under the Softwood Lumber Agreement ("SLA") over its concern that the Province has misapplied or altered its timber pricing rules and as a result has charged too low a price for certain timber harvested on public lands in the BC interior. In August, 2011 the US filed a detailed statement of claim with the arbitration panel. Canada delivered its initial response to the US claim in November 2011. On July 18, 2012 the arbitration panel dismissed in their entirety the claims of the United States that Canada and BC had misapplied its timber pricing practices and so circumvented the SLA.

The US Lumber Coalition (the "Coalition") has claimed that the BC government has been undercharging the coastal forestry industry for timber harvested on crown lands and is questioning the accuracy of BC's Coast market pricing system ("MPS"). The Coalition has taken the issue to the office of the US Trade Representative ("USTR"), which has in turn written to the Ministry of Forests to enquire as to the status of the update of the Coast MPS. The Coast MPS was introduced in 2004 and updated in 2007 and 2009. There is no time requirement in the SLA as to when updates occur, however, on July 1, 2012 the Coast MPS was updated and, consistent with the Softwood Lumber Agreement, the USTR has been informed. Due to the preliminary nature of this situation there is no evidence of the existence of any potential liability, and so no amount has been provided for in the September 30, 2012 financial statements.

17. Financial Instruments

As at September 30, 2012, the Company had outstanding obligations to sell an aggregate JPY 1,350 million at an average rate of JPY 81.07 per CAD with maturities through December 31, 2012, and an aggregate US $21.0 million at an average rate of US $0.9816 per CAD with maturities through December 31, 2012. All foreign currency gains or losses related to currency forward contracts to September 30, 2012 have been recognized in revenue for the period and the fair value of these instruments at September 30, 2012 was a net liability of $0.5 million, which is included in accounts payable and accrued liabilities on the statement of financial position (December 31, 2011: net liability of $2.8 million). A net loss of $0.8 million was recognized on contracts which were settled in the nine months ended September 30, 2012 (2011: net gain of $1.0 million), which was included in revenue for the period.

18. Other Income (Expenses)

Other income of $1.1 million in the third quarter of 2012 related primarily to proceeds received from the Province as final compensation resulting from the creation of new protective areas in the Company's Haida Gwaii and Central Coast operating areas. The expense of $1.9 million in the third quarter in 2011 was due to impairment losses taken on intangible and other assets related to the sale of Tree Farm License 60 ("TFL 60").

(Tabular amounts expressed in millions of Canadian dollars)

Other income of $3.7 million for the nine months ended September 30, 2012 related primarily to net gains on asset sales, with the most significant being the sale of TFL 60 to Taan Forest Limited Partnership ("Taan") during the second quarter. Taan is a partnership of the Council of the Haida Nation and Haida Enterprise Corporation, the business arm of the Haida Nation. Under the terms of the sale, Western received net proceeds of approximately $12.2 million, of which $2.6 million had previously been received in the first quarter of 2012, and certain ongoing rights to cedar logs harvested by Taan. Taan assumed substantially all of the obligations of Western on Haida Gwaii. The assets and liabilities associated with this sale were previously presented on the consolidated statements of financial position as held for sale.

Other expenses of $2.5 million for the nine months ended September 30, 2011 comprised net losses on non-core asset sales of $1.1 million, a gain on the sale of an equity interest in certain real estate properties of $2.4 million, an expense incurred of $2.5 million to secure amendments to the terms of certain contractual arrangements, $1.7 million in impairment losses relating to TFL 60, and other items totaling income of $0.4 million. The most significant non-core asset sale during the period was a 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.

19. Expenses by Function

	Three months ended September 30		Nine months ended September 30	
	2012	2011	2012	2011
Administration	$ 4.8	$ 4.0	$ 15.3	$ 12.4
Distribution expenses	22.1	27.9	79.1	81.3
Cost of goods sold	189.9	192.4	583.4	509.3
	$ 216.8	$ 224.3	$ 677.8	$ 603.0

Distribution expenses comprise selling expenses, freight costs and export taxes.

20. Other Expense Information

The Company recorded total employee compensation costs for the nine months ended September 30, 2012 of $144.8 million (2011: $138.7 million).

Total amortization expense for the three and nine months ended September 30, 2012 was $6.2 million and $19.9 million, respectively (2011: $6.0 million and $18.3 million, respectively).

21. Assets Held for Sale

The assets and liabilities related to TFL 60 were presented in the December 31, 2011 and March 31, 2012 statements of financial position as a disposal group held for sale following the Company reaching an agreement on October 11, 2011 to sell TFL 60 to Taan Forest Limited Partnership ("Taan"). During the second quarter of 2012, this sale was completed (see Note 18).

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