CONIFEX

CONIFEX TIMBER INC.
THIRD QUARTER 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

Dated as of November 1, 2013

*This interim Management's Discussion and Analysis ("**MD&A**") provides a review of the financial performance of Conifex Timber Inc. for the quarter ended September 30, 2013 relative to the quarters ended June 30, 2013 and September 30, 2012, the Company's financial condition and future prospects. This interim MD&A should be read in conjunction with the unaudited condensed consolidated interim financial statements and accompanying notes of Conifex for the quarters ended September 30, 2013 and 2012, as well as the 2012 annual MD&A and the December 31, 2012 audited consolidated financial statements and notes thereon which are filed on SEDAR at www.sedar.com.*

In this interim MD&A, reference is made to "EBITDA". EBITDA represents earnings before interest, taxes, depreciation and amortization, as well as before deductions for non-cash charges related to employee compensation and changes in the balance sheet carrying value of convertible debentures and other investments. The Company discloses EBITDA as it is a measure used by analysts and by Conifex's management to evaluate the Company's performance. As EBITDA is a non-GAAP measure, it may not be comparable to EBITDA as calculated by others. In addition, as EBITDA is not a substitute for net earnings, readers should consider net earnings in evaluating the Company's performance.

Unless otherwise noted, all monetary references in this interim MD&A are in Canadian dollars.

*References in this interim MD&A to "**Conifex**" and the "**Company**" mean Conifex Timber Inc., together with its subsidiaries, unless the context otherwise requires.*

FORWARD-LOOKING STATEMENTS

This interim MD&A contains certain forward-looking information that reflects the current views and/or expectations of the Company with respect to its expectations, beliefs, assumptions, estimates and forecasts about its business and the industries and markets in which it operates. The reader is cautioned that statements comprising forward-looking information are not guarantees of future performance and involve known and unknown risks, uncertainties, assumptions and other factors which are difficult to predict and that may cause actual results or events to differ materially from those anticipated in such forward-looking information. Accordingly, readers should not place undue reliance on forward-looking information. Examples of such forward-looking information that may be contained in this document include statements regarding: growth and future prospects of our business; our expectation for the export tax rate assessed on lumber shipments to the U.S.; our expectation for mill net realizations; that the Company will successfully negotiate and sign a new collective labour agreement with its unionized employees; our perceptions of the industry and markets in which we operate and anticipated trends in such markets and in the countries in which we do business; benefits that *may accrue to the Company as a result of certain capital expenditure programs, such as the lumber segment capital plan, equipment upgrades and maintenance shutdowns; and the anticipated benefits, cost, timing and completion dates for projects, including the Bioenergy Project.*

Assumptions underlying the Company's expectations regarding forward-looking information contained in this MD&A include, among others: that the Company will be able to effectively market its products; that the Company will conclude a new collective labour agreement on satisfactory terms; that the U.S. housing market will continue to improve; that there will be no further delays and disruptions affecting the completion of the Bioenergy Project and that the Company will be able to commence timely delivery of power therefrom; that softwood lumber will experience improved and sustained demand in the marketplace at favourable prices; that the export tax rate on U.S. lumber shipments will be less than the maximum rate; that the Company will be able to dynamically respond to shifts in demand among its major markets; the general stability of the economic, political and regulatory environments within the countries where the Company conducts operations; the ability of the Company to obtain financing (if necessary) on acceptable terms or at all; that interest and foreign exchange rates will not vary materially from current levels; and that our mills and equipment will operate at expected levels.

Persons reading this MD&A are cautioned that statements comprising forward-looking information are only predictions, and that the Company's actual future results or performance are subject to certain risks and uncertainties including, without limitation: those relating to potential disruptions to production and delivery, including as a result of equipment failures, labour issues, the complex integration of processes and equipment and other factors; labour relations; failure to meet regulatory requirements; changes in the market; potential downturns in economic conditions; fluctuations in the price and supply of required materials, including log costs; fluctuations in the market price for products sold; foreign exchange fluctuations; trade restrictions or import duties imposed by foreign governments; availability of financing (as necessary); and other risk factors detailed in our Annual Information Form dated April 17, 2013 available on SEDAR at www.sedar.com and other filings with the Canadian securities regulatory authorities. These risks, as well as others, could cause actual results and events to vary significantly. The Company does not undertake any obligation to update any forward-looking information, except as required by applicable securities law.

SIGNIFICANT DEVELOPMENTS

Completion of $30 million senior secured financing

On September 18, 2013, the Company completed a senior secured financing agreement (the "Notes Financing") under the terms of which the Company issued promissory notes in the aggregate principal amount of $30 million. The terms of the Notes Financing and additional consideration provided is discussed under "Financing Activities and Liquidity". The Company intends to use the net proceeds of the notes for general corporate purposes, including primarily for strategic capital projects to enhance and improve efficiencies and production in its lumber segment manufacturing facilities.

Mackenzie Bioenergy Project developments

During the third quarter of 2013, management finalized its capital expenditure budget for its Mackenzie Bioenergy Project at approximately $98 million including a $6 million general contingency. In September 2013, the Company announced commitment for funding of the

Bioenergy Project for an aggregate of $103 million, including approximately $80 million as a development and construction loan (the “Project Financing”). The Project Financing is expected to be completed in the near term. The Company recommenced construction of the Bioenergy Project in mid-September. Further discussion of these developments can be found below under “Bioenergy Segment”.

Conifex’s Collective Agreement with the United Steelworkers (USW)

The Company’s collective labour agreement with the USW expired on June 30, 2013. Conifex anticipates entering into discussions with the USW during the fourth quarter of 2013. Although we have not experienced any work stoppages in the past and do not expect any work stoppages now, there can be no assurance that we will be able to negotiate an acceptable collective agreement with our employees. Any new collective labour agreement will be retroactive to July 1, 2013.

Appointments to Conifex board and management team

<u>Appointment of Patrick Bell as Director</u>
In August 2013, the Company announced the appointment of Patrick Bell to its Board of Directors. During his political career, Mr. Bell served three terms in the BC Legislature and held a number of high profile positions with the Provincial Government, including Minister of Jobs, Tourism and Skills Training, Minister of Forests and Range, and Minister of Agriculture. Mr. Bell’s entrepreneurial career involved interests in a variety of businesses, including a logging company and a trucking company. Earlier in his career, Mr. Bell worked in the hospitality industry at a corporate level and remains involved with the organization as a franchisee.

<u>Appointment of Hans Thur as Senior Vice President, Marketing</u>
In August 2013, the Company announced the appointment of Hans Thur as Senior Vice President, Marketing and President of its wholly-owned subsidiary Conifex Fibre Marketing Inc. effective in September 2013. Mr. Thur’s background includes extensive marketing, sales and global supply chain management experience with a leading North American lumber manufacturer. Mr. Thur is familiar with the softwood lumber wholesale and distribution business through direct experience gained earlier in his career.

SUMMARY OF OPERATING RESULTS AND FINANCIAL POSITION

CONSOLIDATED OPERATING RESULTS

(millions of dollars except share and per share amounts)	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
Sales -Lumber	56.1	54.8	169.5	46.1	131.1
- By-products	4.9	5.6	15.0	5.1	15.2
- Logistics services	4.2	4.0	11.4	3.2	11.3
Total Sales	65.2	64.4	195.9	54.4	157.6
Operating income (loss)	0.7	3.3	10.6	(2.8)	(10.5)
Net income (loss)	(0.1)	2.4	8.5	(3.7)	(12.6)
Net income (loss) per share - basic	(0.01)	0.12	0.41	(0.19)	(0.68)
Net income (loss) per share - diluted	(0.01)	0.12	0.41	(0.19)	(0.68)
EBITDA	2.8	4.8	16.9	(0.5)	(3.7)
Shares outstanding - end of period (millions)	20.8	20.8	20.8	19.4	19.4
Shares outstanding - weighted average (millions)	20.8	20.8	20.8	19.4	18.7
Statistics					
Lumber shipments - Conifex product (MMfbm)	129.3	119.2	368.3	107.5	334.0
Lumber shipments - wholesale (MMfbm)	17.6	12.3	47.1	19.2	57.4
Lumber production (MMfbm)	123.0	135.8	383.0	102.8	316.1
Average exchange rate - US$/Cdn$ (1)	0.963	0.977	0.977	1.005	0.998
Average WSPF 2x4 #2&Btr lumber price (US$) (2)	$ 328	$ 334	$ 351	$ 301	$ 288
Average WSPF 2x4 #2&Btr lumber price (Cdn$) (2)	$ 341	$ 342	$ 359	$ 299	$ 288

(1) Source: Bank of Canada website www.bankofcanada.ca
(2) Source: Random Lengths Publications Inc.

(millions of dollars)	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
Net income (loss)	(0.1)	2.4	8.5	(3.7)	(12.6)
Add: Interest expense	0.5	0.4	1.7	0.5	1.6
Depreciation and amortization	2.3	2.1	6.4	1.9	5.6
Deferred union payroll liability	(0.2)	(0.3)	(0.8)	-	-
Share based compensation	0.2	(0.1)	0.3	0.4	0.7
Accretion of convertible debentures	0.2	0.3	0.8	0.3	0.8
Loss of disposal of assets	-	-	-	0.1	0.3
EBITDA*	2.8	4.8	16.9	(0.5)	(3.7)

*May not total exactly due to rounding.

Overview

For the quarter ended September 30, 2013, the Company recorded a net loss of $0.1 million or $0.01 per share on sales of $65.2 million compared to net income of $2.4 million or $0.12 per share on sales of $64.4 million during the second quarter of 2013, and net loss of $3.7 million or $0.19 per share on sales of $54.4 million during the third quarter of 2012. Net income for the first nine months of 2013 was $8.5 million or $0.41 per diluted share compared to a net loss of $12.6 million or $0.68 per share over the same period last year.

Third quarter 2013 EBITDA of $2.8 million was comprised of lumber segment EBITDA of $4.0 million offset by negative bioenergy segment EBITDA of $0.1 million and corporate costs and other items of $1.1 million. Lumber segment EBITDA declined by $6.7 million over the previous quarter and improved by $3.0 million over the third quarter of 2012. EBITDA related to the bioenergy segment was consistent with comparative quarters. Corporate costs and other items were lower in the third quarter of 2013 compared to the second quarter of 2013 and compared to the third quarter of 2012. The increase in year to date corporate costs compared to the same period last year was largely attributable to accruals related to the Company's variable compensation plan during the first six months of 2013.

At September 30, 2013, the Company had $29.3 million cash and cash equivalents on hand compared to $14.1 million at December 31, 2012. An increase of $6.3 million in lumber segment working capital over the previous quarter was attributable primarily to the return to more normalized log inventory levels. The Company ended the third quarter of 2013 with net debt of $17.7 million and a net debt to capitalization ratio of 13%.

REVIEW OF OPERATING RESULTS BY BUSINESS SEGMENT

Operating Results by Business Segment

(millions of dollars)	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
Revenue					
Lumber	65.2	64.4	195.9	54.4	157.6
Bioenergy	-	-	-	-	-
	65.2	64.4	195.9	54.4	157.6
Net Income (Loss)					
Lumber	1.9	4.7	15.3	(1.2)	(6.5)
Bioenergy	(0.1)	(0.2)	(0.4)	(0.2)	(0.8)
Corporate costs and other items	(1.9)	(2.1)	(6.4)	(2.2)	(5.3)
	(0.1)	2.4	8.5	(3.7)	(12.6)
EBITDA					
Lumber	4.0	6.7	21.2	1.0	(0.1)
Bioenergy	(0.1)	(0.2)	(0.4)	(0.3)	(0.8)
Corporate costs and other items	(1.1)	(1.7)	(3.9)	(1.2)	(2.8)
	2.8	4.8	16.9	(0.5)	(3.7)

*May not total exactly due to rounding.

Lumber Segment

Overview

WSPF 2x4 #2 & Btr ("WSPF") prices averaged approximately US$ 328 during the third quarter of 2013 and reflected a decline of 2% from the second quarter of 2013 and an improvement of 9% over the third quarter of 2012[1]. The decline of 2% in average U.S. benchmark prices was offset by a corresponding weakness in the Canadian dollar and resulted in flat quarter over

[1] Prices as quoted in Random Lengths Publications Inc.

quarter average benchmark prices expressed in Canadian dollars of approximately $341.[2] Year to date WSPF prices averaged US$ 351 and represented an increase of approximately 22% over the same period last year.

The modest 2% quarter over quarter change in the average benchmark prices belies the considerable volatility exhibited during the second and third quarters of 2013. WSPF prices averaged US$ 368 during the first six weeks of the second quarter compared to an average of US$ 301 during the closing six weeks. During the first six weeks of the third quarter, WSPF prices averaged US$315 then steadily improved to average US$340 during the last six weeks of the quarter. The effect of shipment lags between the dates orders are transacted and shipped is more pronounced on sales to export market than on sales to the North American market because of longer transit times. Thus a significant portion of orders shipped to export markets during the third quarter of 2013 would likely have been priced at lower relative values than would be indicated by average benchmark prices.

During the third quarter of 2013, shipments to export markets represented approximately 67% of total shipments, comprised of shipments to China of 58% and Japan of 9%. Approximately 22% of total shipments went to the U.S. and the remaining 11% to Canada. Compared to the second quarter of 2013, average unit mill net realizations improved on shipments to Japan and Canada by 6% and 4% respectively but declined by 10% on shipments to China and the U.S. Compared to the third quarter of 2012, average unit mill net realizations improved from all our key markets, most notably by 54% from Japan.

Shipments of Conifex produced lumber totalled approximately 129 million board feet during the third quarter of 2013 and represented an increase of approximately 8% over the previous quarter and 20% over the third quarter of 2012. Wholesale lumber shipments increased by approximately 5 million board feet over the previous quarter primarily as a result of stronger demand from the Chinese market.

During the third quarter of 2013, lumber production totalled 123 million board feet compared to 136 million board feet in the previous quarter and 103 million board feet in the third quarter of 2012. The decline of 10% from the previous quarter was attributable primarily to a short term decline in productivity related to capital projects undertaken at both mills that were concentrated in the last month of the quarter. Hourly production at both locations returned to expected levels following the completion of these projects. Current year to date production totalled 383 million board feet, an increase of 21% over the same period last year.

Annualized operating rates were approximately 66% for the third quarter of 2013 compared to 73% for the second quarter of 2013 and 55% for the third quarter of 2012.

Compared to the second quarter of 2013, overall unit log costs during the third quarter of 2013 increased by approximately 2% while lumber recoveries remained consistent. Unit log costs increased by 23% over the third quarter of 2012 while lumber recoveries improved by 9%.

The export tax rate assessed on shipments of lumber to the U.S. averaged 5% during the third quarter of 2013, and slightly less than 2% during the first nine months of 2013, compared to an average of 8.33% during the third quarter of 2012 and 12.2% during the first nine months of 2012.

[2] Based on average monthly rates as quoted on Bank of Canada website www.bankofcanada.ca

The Company recorded net income of $1.9 million in its lumber segment on sales of $65.2 million for the third quarter of 2013 compared to net income of $4.7 million on sales of $64.4 million for the previous quarter and a net loss of $1.2 million on sales of $54.4 million for the same quarter last year. Lumber segment year to date net income was $15.3 million on sales of $195.9 million compared to a net loss of $6.5 million on sales of $157.6 million for the first nine months of 2012.

EBITDA in this segment was $4.0 million for the third quarter of 2013 compared to $6.7 million for the previous quarter and $1.0 million for the third quarter of 2012. Lumber segment EBITDA was $21.2 million for the first nine months of 2013 compared to negative $0.1 million for the same period last year.

The decline in lumber segment net income of $2.8 million compared to the second quarter of 2013 was primarily attributable to lower mill net realizations and, to a lesser extent, to modest increases in log costs and unit cash conversion costs. Compared to the third quarter of 2012, lumber segment net income increased by $3.1 million as the benefits of an 8% improvement in unit mill net realizations from higher lumber prices and a lower export tax rate, and a 14% reduction in unit cash conversion costs more than offset higher log costs.

<u>Sales</u>
Shipments of Conifex produced lumber totalled approximately 129 million board feet during the third quarter of 2013, an increase of approximately 8% over the previous quarter and 20% over the third quarter of 2012. The increase in shipments over the previous quarter reflects the intentional finished goods inventory build late in the previous quarter in anticipation of heightened activity and relatively favourable mill net realizations expected from offshore markets during the third quarter of 2013. Wholesale lumber shipments increased by approximately 5 million board feet to more typical levels compared to the previous quarter on the strength of improved demand from the Chinese market for certain specialized products manufactured by third party vendors. Shipments of Conifex produced lumber during the first nine months of 2013 totalled 368 million board feet with the increase of 10% over the same period last year attributable to higher production volumes. Overall year to date shipments including wholesale lumber increased by 6% from last year and totalled 415 million board feet.

Gross revenues from lumber shipments totalled $56.1 million, an increase of 2% over the second quarter of 2013, primarily resulting from a 12% increase in total shipment volumes offset by a decline in overall unit gross sales realization of approximately 8%. Gross revenues increased by 22% over the third quarter of 2013 primarily due to higher shipment volumes of 16% and a 5% improvement in unit gross sales realizations. Year to date gross revenues increased by 29% over the first nine months of 2012 mainly as a result of a 6% increase in shipment volumes and an improvement in unit gross sales realizations approaching 22%.

During the third quarter of 2013, shipment volumes to Japan represented 9% of total Company shipments and contributed 15% of total mill net realizations. Shipments to China increased to 58% of total shipments in response to the relatively higher unit mill net realizations available from that market on certain products compared to the North American market and the increase of wholesale lumber shipments to normalized levels. Shipments to Canada and the U.S. represented 11% and 22% respectively of total shipment volumes.

Compared to the second quarter of 2013, average unit mill net realizations improved on shipments to Canada and Japan by 4% and 6% respectively but declined by 10% on shipments to China and the U.S. Compared to the third quarter of 2012, unit mill net realizations improved from all our geographic markets with increases ranging from 54% from Japan, to 19% from Canada, 10% from the U.S. and 6% from China. Overall unit mill net realizations declined by 10% from the previous quarter and improved by 8% from the third quarter of 2012. Unit mill net realizations on shipments to the U.S. during the third quarters of 2013 and 2012 were adversely impacted by an average export tax of 5% and 8.33% respectively.

The table below shows the percentage of net lumber revenue earned from and volume shipped to each geographic market.

	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
By Revenue (net of freight)					
Canada	12%	13%	10%	15%	16%
USA	23%	46%	41%	54%	41%
Japan	15%	14%	13%	5%	5%
China and other	50%	27%	36%	26%	38%
	100%	100%	100%	100%	100%
By Shipment Volume					
Canada	11%	14%	11%	15%	15%
USA	22%	44%	38%	53%	39%
Japan	9%	10%	9%	4%	4%
China and other	58%	32%	42%	28%	42%
	100%	100%	100%	100%	100%

Revenue from chips and other residuals in the third quarter of 2013 totalled $4.9 million. The decline of 12% from the previous quarter was primarily attributable to an 11% increase in unit chip prices, which are related to fluctuations in NBSK pulp prices, offset by a 23% reduction in shipment volumes largely resulting from lower production volumes.

Revenue from the provision of freight and logistics services to third parties during the third quarter of 2013 totalled $4.2 million and represented an increase of 5% over the previous quarter and 32% over the third quarter of 2012.

Production and Operations

Lumber production totalled 123 million board feet in the third quarter of 2013 compared to 136 million board feet in the previous quarter and 103 million board feet in the third quarter of 2012. Production volumes during the third quarter of 2013 were impacted primarily by disruptions from capital projects undertaken at both mills which were concentrated in the last month of the quarter. The Company undertook capital projects totalling $4.9 million during the quarter. The upgrades did not involve any shutdowns, but hourly productivity levels were reduced as a result of operating under test conditions and the measured ramp up to normal production levels. Hourly production at both mills returned to expected levels following the completion of the upgrades. Production levels during the third quarter of 2012 were negatively impacted by planned curtailments for dust mitigation and other safety related maintenance and capital upgrades. The downtime represented approximately 5% of typical total quarterly operating hours. Current year to date production totalled 383 million board feet, an increase of 21% over the same period last year.

Average hourly production during the third quarter of 2013 was approximately 10% less than the previous quarter, when the Company experienced record production levels, but improved by 8%

over the third quarter of 2012. Average hourly production on a year to date basis has improved by 15% over the same period last year. The Company expects further revenue and productivity gains from its ongoing capital improvement initiatives, including those completed during the recent quarter.

Annualized operating rates were approximately 66% for the third quarter of 2013, compared to 73% for the second quarter of 2013 and 55% for the third quarter of 2012. We calculate operating rates based on production volumes during the period and total estimated annual production capacity of 745 million board feet.

Overall unit log costs during the third quarter of 2013 increased by approximately 2% over the previous quarter as the effects of a considerable increase in stumpage rates were not reflected until late in the quarter generally due to the lag between harvesting of the logs and delivery to the mill sites. Because of this lag effect, the Company expects the impact of higher third quarter stumpage costs to be reflected in the fourth quarter. Lumber recovery factors remained consistent during the third and second quarter of 2013. Compared to the third quarter of 2012, an increase in unit log costs of 23% was offset by an improvement of 9% in lumber recovery and resulted in a net unit log cost increase of 14%. The increase in delivered log costs is generally attributable to costs associated with increased stumpage rates, logging and hauling rates, and purchased log costs.

Unit cash conversion costs during the third quarter of 2013 increased by only 2% over the previous quarter despite a 10% reduction in production levels. Unit cash conversion costs improved by 14% compared to the third quarter of 2012 with the improvement largely attributable to productivity gains. Cost of goods sold also includes costs related to shipments of wholesale lumber and freight procurement costs related to third party logistics revenue.

The moderate fluctuation in freight and distribution costs related to shipments of Conifex produced lumber on a per unit basis during the comparative quarters was attributable to the slightly weaker Canadian currency in the third and second quarter of 2013 compared to the second quarter of 2012 and changes in shipment patterns amongst the various geographical markets.

The export tax rate applicable on shipments to the U.S. averaged 5% and resulted in an export tax expense of $0.4 million during the third quarter of 2013 compared to an export tax rate of zero percent during the previous quarter, and export tax expense of $1.3 million based on an average rate of 8.33% during the third quarter of 2012.

Bioenergy Segment

<u>Background</u>

In March 2011, the Company initiated the Bioenergy Project at its Mackenzie sawmill site, originally scheduled for commercial production of electricity in the third quarter of 2013. The planned Bioenergy Project consists of constructing a 36 megawatt biomass power plant in Mackenzie, British Columbia adjacent to our currently idled site I sawmill complex within an existing building with supporting infrastructure that formerly housed a newsprint production facility. The Bioenergy Project is being developed by the Company's wholly-owned subsidiary, Conifex Power Limited Partnership ("Conifex Power").

In late 2012, with major equipment on site and initial construction completed as planned before winter, the Company decided that, in order to further continued development of the project and secure satisfactory long-term financing, essential engineering and equipment procurement activities would continue but installation and construction activities would be temporarily suspended. The Bioenergy Project was approximately 30% complete and on budget and on time when construction activities were temporarily suspended.

During the first six months of 2013, the Company undertook a detailed assessment of the impact of the suspension of construction activity on the project schedule and capital expenditure budget. Subsequent to the completion of further engineering and design work on the project to refine scope and re-evaluate key vendor contracts, and recalibration of the project schedule, the management prepared capital expenditure budget was revised to approximately $98 million including a $6 million general contingency. To facilitate these development activities, in February 2013, Conifex Power completed a $5 million senior secured financing. The notes were fully repurchased in September 2013.

Commitment for financing for the Bioenergy Project

In September 2013, Conifex Power accepted commitment letters from a syndicate of institutional lenders led by a Canadian chartered bank for the Project Financing for the Bioenergy Project. The Project Financing is for an aggregate of $103 million and includes approximately $80 million (the "Loan Facility") as a development and construction loan for the Bioenergy Project. The Loan Facility will consist of a construction loan which will mature approximately 14 months from the closing date and convert into an amortized term loan having a term of 5 years upon satisfaction of certain conditions, including substantial completion of construction of the Bioenergy Project. The balance of the Project Financing will be in the form of a letter of credit facility primarily to secure certain obligations of Conifex Power under its existing load displacement agreement and a $1.75 million revolving operating facility.

The Project Financing is expected to be completed in the near term and will be subject to customary closing conditions for a project financing of this type, including, among others completion of definitive documentation, which shall contain customary representations, warranties and covenants.

Recommencement of Bioenergy Project

Conifex Power recommenced construction of the Bioenergy Project in September 2013. The power generation plant is currently expected to commence commercial operations in the third quarter of 2014. A material delay in completing the Project Financing could delay the overall development of the Bioenergy Project, including the currently anticipated commercial operation date. At this time, there can be no assurance that the Project Financing will be completed on the anticipated schedule, if at all.

Capital expenditures related to the Bioenergy Project totalled $6.4 million during the first nine months of 2013 and $36.0 million since the inception of the project. The Company does not intend to commit any significant further capital to the project on a permanent basis.

The net loss reported in the bioenergy segment in each of the comparative periods arises primarily from professional fees and costs related to holding idled facilities such as insurance premiums and property tax.

Corporate costs and other items

(millions of dollars)	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
Corporate costs	1.0	1.2	3.9	1.0	2.5
Borrowing costs	0.5	0.4	1.7	0.5	1.6
Foreign exchange loss	0.2	0.2	-	0.4	0.5
Accretion of convertible debenture	0.2	0.3	0.8	0.3	0.7
	1.9	2.1	6.4	2.2	5.3

The increase in year-to-date corporate costs is primarily attributable to accruals related to the Company's variable compensation plan during the first six months of 2013. The accruals for variable compensation may be paid at the end of the fiscal year dependent upon the degree of improvement in the Company's operating results in the current year. Borrowing costs are comprised of interest expense and amortization of costs related to debt placement and issuance of share purchase warrants. The fluctuation in foreign exchange loss represents net translation and transaction gains or losses arising from conversion of U.S. denominated assets and liabilities into Canadian dollars at the prevailing exchange rates.

Income tax

Conifex has not recognized current income tax expense during the first nine months of 2013 as the Company had non-capital loss carry forwards totalling approximately $31.6 million as at December 31, 2012. Although the Company expects to realize the full benefits of the loss carry-forwards and other deferred tax assets, due to the cyclical nature of the wood products industry and the economic conditions over the last several years, the Company has not recognized the benefits of its deferred tax assets available to reduce future taxable income.

FINANCIAL POSITION AND CASH FLOW

SELECTED CASH FLOW ITEMS

(millions of dollars)	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
Operating Activities					
Cash provided (used) before working capital changes	2.7	4.5	18.0	(1.1)	(3.1)
Non - cash working capital change	(6.3)	8.8	(5.0)	1.8	(2.9)
Cash provided from (used in) operating activities	(3.6)	13.3	13.0	0.7	(6.0)
Investing Activities					
Additions to property, plant, equipment	(8.8)	(5.7)	(19.2)	(8.2)	(20.5)
Proceeds on disposal of assets held for sale	-	-	-	-	0.4
Cash used in investing activities	(8.8)	(5.7)	(19.2)	(8.2)	(20.1)
Financing Activities					
Net proceeds from private placements	-	-	-	-	26.9
Proceeds from (repayment of) secured notes	25.0	(12.0)	18.0	-	-
Proceeds from revolving credit facility	7.0	-	7.0	-	-
Proceeds from incentive funding	-	-	-	3.3	3.3
Repayment of CAF loan	(0.5)	(0.4)	(1.3)	(0.4)	(1.3)
Interest expense paid	(0.1)	(1.3)	(2.3)	(0.1)	(0.8)
Cash provided from (used in) financing activities	31.4	(13.7)	21.4	2.8	28.1
Change in cash	19.0	(6.1)	15.2	(4.7)	2.0

Cash provided from (used in) non-cash working capital items

(millions of dollars)	Q3 2013	Q2 2013	YTD 2013	Q3 2012	YTD 2012
Trade and other receivables	(1.3)	5.4	0.7	(1.6)	(7.2)
Inventories	(11.3)	7.0	(14.6)	2.1	(0.8)
Accounts payable and accrued liabilities	4.0	(1.4)	8.6	0.7	4.8
Other	2.3	(2.2)	0.3	0.6	0.3
	(6.3)	8.8	(5.0)	1.8	(2.9)

The Company’s improvement in operating results generated positive cash flow before working capital changes of $2.7 million in the third quarter of 2013; $4.5 million in the previous quarter and $18.0 million year-to-date, compared to cash usage of $1.1 million in the third quarter of 2012 and $3.1 million during the first nine months of 2012. The net change in non-cash working capital consumed cash of approximately $6.3 million in the third quarter of 2013 compared to cash generation of $8.8 million in the previous quarter and $1.8 million during the third quarter of 2012. The increase in working capital during the third quarter of 2013 was largely attributable to the build in log inventories to normalized levels after being drawn to seasonal lows at the end of the previous quarter. The overall inventory levels were somewhat offset by a reduction in finished goods inventory as current quarter shipments outpaced production.

Investments in capital items on a cash basis totalled $8.8 million during the third quarter of 2013, $5.7 million during the second quarter of 2013, and $8.2 million during the third quarter of 2012. The Company invested $19.2 million in capital assets during the first nine months of 2013 compared to $20.5 million during the same period last year. Capital expenditures during the first nine months of 2013 consisted of $8.2 million in the lumber and corporate segment primarily on mobile equipment, items related to major maintenance and replacement, safety and asset protection, and relocation of the corporate office, and $11.0 million on the Bioenergy Project of which $4.6 million had been capitalized during prior periods or payable in subsequent periods. Additions to property, plant and equipment during the first nine months of 2012 included $10.2 million on the Bioenergy Project, $3.0 million on the automated lumber grading system at Mackenzie and $4.6 million primarily on initiatives related to workplace safety and asset protection.

Financing activities during the third quarter of 2013 consisted of gross proceeds of the Notes Financing of $30 million; net borrowings under the revolving credit facility of $7.0 million; full repurchase of the 12% senior secured notes that were issued by Conifex Power in February 2013 in the principal amount of $5.0 million; quarterly repayment of the Community Adjustment Fund ("CAF") loan of $0.4 million and borrowing costs on a cash basis of $0.1 million. Financing activities during the second quarter of 2013 consisted of full repayment of the 12% senior secured notes that were issued in December 2011 in the principal amount of $12 million; quarterly repayment of the CAF loan of $0.4 million and borrowing costs of $1.3 million. Borrowing costs paid during the second quarter of 2013 included interest on the senior secured notes; semi-annual interest payment on the convertible notes; and financing costs related to the completion of the $25 million revolving credit facility. Financing activities during the first nine months of 2012 consisted of net proceeds from the equity financing of $26.9 million during the first quarter, receipt of $3.3 million incentive funds related to the Load Displacement Agreement during the third quarter, repayment of the CAF loan of $1.3 million and payment of interest expenses of $0.8 million.

During the first nine months of 2013, cash and cash equivalents increased by $15.2 million compared to an increase of $2.0 million during the first nine months of 2012. The Company had cash and cash equivalents on hand of $29.3 million at September 30, 2013 compared to $14.1 million at December 31, 2012 and $14.8 million at September 30, 2012. The Company ended the third quarter of 2013 with net debt of $17.7 million and net debt to capitalization ratio of 13% compared to $8.6 million and 7% respectively in the previous quarter.

FINANCING ACTIVITIES AND LIQUIDITY

Completion of $30 million senior secured financing

On September 18, 2013, the Company completed the Notes Financing pursuant to which the Company issued promissory notes (the "Notes") to investment funds managed by Vertex One Asset Management Inc. in the aggregate principal amount of $30 million.

The Notes have a term of four years and bear interest at a rate of 8% per annum. The Company may redeem the Notes, in whole or in part, at any time on or after four months from the issue date of the Notes upon 15 days' notice and payment of interest accrued on the amount redeemed to the date of redemption, but otherwise at par.

As additional consideration for the Notes Financing, the Company issued common share purchase warrants entitling the holders to purchase up to an aggregate of 1,060,000 common shares of the unissued capital stock of the Company at a price of $8.25 per share for a period of four years following issuance.

The Company intends to use the net proceeds from the Notes for general corporate purposes, including primarily for strategic capital projects to enhance and improve the efficiencies and production in its lumber segment manufacturing facilities.

Repayment of 12% senior secured notes

On September 18, 2013, the Company repurchased in full the 12% promissory notes in the aggregate principal amount of $5 million issued by Conifex Power in February 2013.

Liquidity

The Company's current principal sources of funds are cash flow from operations, cash on hand, and borrowing availability under its existing revolving credit facility. The Company's current principal uses of funds consist of operating and capital expenditures and repayment of debt.

As part of its overall strategy, the Company may acquire businesses or additional assets from time to time as such opportunities arise. As a result, the Company may require substantial additional capital resources. The Company expects such additional capital resources will be generated from debt financing and/or the sale of equity securities.

The Company's working capital levels fluctuate throughout the year and are affected by changes in operating rates, changing sales patterns, seasonality and the timing of receivables and the payment of payables and expenses. The Company's fibre inventories exhibit seasonal swings as the Company increases log inventories during the winter months to help ensure adequate supply of fibre to its mills during the spring months. Changes in sales volume and price can affect the level of receivables and influence overall working capital levels. An increase in shipments to export markets requires carrying a higher level of transit finished goods inventory. Working capital is also required to support third party transactions undertaken by the Company's wholesale lumber and logistics services businesses. The Company believes its management practices with respect to working capital conform to common industry practices.

The Company's existing $25 million revolving credit facility, completed in April 2013, provides an additional source of funds to support the Company's considerable investment in non-cash working capital, consisting primarily of accounts receivable and inventory, and to further optimize marketing and manufacturing activities in its lumber segment.

The Company's lumber segment capital plan totalling $18.7 million is expected to be implemented during the current year and the first half of 2014. The Company intends to fund its current and future capital improvement program primarily from internally generated cash flows and the net proceeds from the recently completed Notes Financing.

The Company, through its wholly-owned subsidiary, Conifex Power, has secured funding for its Bioenergy Project as discussed under "Bioenergy Segment", which it expects to complete in the near term.

SELECTED QUARTERLY FINANCIAL INFORMATION

Quarterly Earnings Summary	2013			2012				2011
(millions of dollars except share and per share amounts)	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Sales -Lumber	56.1	54.8	58.7	53.3	46.1	45.6	39.4	34.0
- By-products	4.9	5.6	4.3	4.4	5.1	5.6	4.5	4.7
- Logistic services	4.2	4.0	3.2	2.3	3.2	4.6	3.5	-
Total Sales	65.2	64.4	66.2	60.0	54.4	55.8	47.4	38.7
Operating income (loss)	0.7	3.3	6.6	(2.4)	(2.8)	(1.6)	(6.2)	(6.8)
Net income (loss)	(0.1)	2.4	6.2	(3.6)	(3.7)	(2.4)	(6.5)	(7.5)
Net income (loss) per share - basic	(0.01)	0.12	0.30	(0.18)	(0.19)	(0.13)	(0.38)	(0.49)
Net income (loss) per share - diluted	(0.01)	0.12	0.29	(0.18)	(0.19)	(0.13)	(0.38)	(0.49)
EBITDA	2.8	4.8	9.2	(0.3)	(0.5)	0.6	(3.8)	(5.2)
Shares outstanding - end of period (millions)	20.8	20.8	20.8	20.7	19.4	19.4	19.4	15.2
Shares outstanding - weighted average (millions)	20.8	20.8	20.7	19.6	19.4	19.4	17.3	15.2
Statistics								
Lumber shipments - Conifex product (MMfbm)	129.3	119.2	119.8	110.2	107.5	111.7	114.8	116.7
Lumber shipments - wholesale (MMfbm)	17.6	12.3	17.2	37.5	19.2	19.4	18.8	-
Lumber production (MMfbm)	123.0	135.8	124.2	108.4	102.8	102.1	111.1	94.9
Average exchange rate - US$/Cdn$ (1)	0.963	0.977	0.991	1.009	1.005	0.990	0.977	0.981
Average WSPF 2x4 #2&Btr lumber price (US$) (2)	$ 328	$ 334	$ 390	$ 335	$ 301	$ 296	$ 267	$ 239
Average WSPF 2x4 #2&Btr lumber price (Cdn$) (2)	$ 341	$ 342	$ 393	$ 332	$ 299	$ 299	$ 267	$ 244

(1) Source: Bank of Canada website www.bankofcanada.ca
(2) Source: Random Lengths Publications Inc.

Reconciliation of EBITDA to Net Loss	2013			2012				2011
(millions of dollars)	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Net income (loss)	(0.1)	2.4	6.2	(3.6)	(3.7)	(2.4)	(6.5)	(7.5)
Add: Interest expense	0.5	0.4	0.8	0.9	0.5	0.5	0.5	0.3
Depreciation and amortization	2.3	2.1	2.0	1.9	1.9	1.8	1.8	1.6
Deferred union payroll liability	(0.2)	(0.3)	(0.3)	(0.2)	-	-	-	(0.1)
Share based compensation	0.2	(0.1)	0.2	0.3	0.4	0.2	0.1	0.2
Accretion of convertible debentures	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Loss on disposal of assets	-	-	-	-	0.1	0.2	-	-
EBITDA*	2.8	4.8	9.2	(0.3)	(0.5)	0.6	(3.8)	(5.2)

*May not total exactly due to rounding.

The Company's financial results are impacted by a variety of market related factors including fluctuation in lumber prices, fluctuations in other commodity prices which impacts by-product revenue and manufacturing costs, and changes in foreign exchange rates. Quarterly trends are also impacted by the seasonal nature of activities such as logging operations and construction and remodelling activity. Other more company specific factors that influence quarterly trends include operating rates and transactions of a non-recurring nature.

The Fort St. James mill and the Mackenzie Site II mill have been operating on a two shift basis since the second quarter of 2011.

On December 31, 2011, the Company internalized its previously outsourced marketing and logistics function by completing the acquisition of a commodity lumber business and a transportation and logistics business. Both of the acquired businesses generate incremental revenue from third party transactions.

Due to the cyclical nature of the forest products industry and the economic conditions over the last several years, the Company has not recognized certain future income tax assets arising from loss carry-forwards available to reduce future taxable income.

OUTLOOK AND STRATEGY

The Company expects improved revenues and positive net income for the closing quarter of 2013. Lumber selling prices have improved and demand is currently solid in each of the Company's markets in North America, China and Japan. Lumber production and shipments are expected to increase because of the benefits of the capital expenditures to upgrade facilities including those incurred in the third quarter.

OUTSTANDING SECURITIES

As at November 1, 2013, the Company had 20,804,039 issued and outstanding common shares, 100,000 options, 817,697 long-term incentive plan awards, 2,210,200 warrants, and stepped rate subordinated convertible promissory notes in the aggregate principal amount of $9,942,000, which notes are convertible into a maximum of 1,242,750 common shares of the Company, excluding any common shares issuable in payment of accrued interest thereon.

CHANGES IN ACCOUNTING POLICY

The Company has adopted the following new and amended standards, along with any consequential amendments, effective January 1, 2013. These changes were made in accordance with the applicable transitional provisions. For a description of the new and revised standards refer to note 2 of our 2012 financial statements.

IFRS 10 – Consolidated Financial Statements, IFRS 11 – Joint Arrangements, IFRS 12 – Disclosure of Interests in Other Entities

The Company has assessed its consolidation conclusion and determined that the adoption of these IFRS's did not result in any changes in the consolidation status of any of its subsidiaries.

IFRS 13 – Fair Value Measurement

The adoption of IFRS 13 did not require any adjustments to the valuation techniques used to measure fair value and did not result in any measurement adjustments.

Amendments to *IAS 1 – Presentation of Financial Statements*

The adoption of the amendments to IAS 1 did not result in any adjustments to other comprehensive income.

RISKS AND UNCERTAINTIES

A discussion of the risks and uncertainties to which the Company is subject is included in the Company's most recent Annual Information Form which is available on www.sedar.com and www.conifex.com.

ADDITIONAL INFORMATION

Additional information about the Company, including its 2012 Annual Information Form, is available on SEDAR at www.sedar.com.