



CONIFEX TIMBER INC. SECOND QUARTER 2010

MANAGEMENT'S DISCUSSION AND ANALYSIS

Dated as of August 30, 2010

This interim Management's Discussion and Analysis ("MD&A") provides a review of the financial performance of Conifex Timber Inc. for the three and six months ended June 30, 2010 relative to 2009, the Company's financial condition and future prospects. This interim MD&A should be read in conjunction with the unaudited interim consolidated financial statements of Conifex for the three and six months ended June 30, 2010 and 2009. On August 27, 2010, the British Columbia Securities Commission granted the Company exemptive relief from the requirement to prepare its financial statements in accordance with Canadian generally accepted accounting principles in order to use International Financial Reporting Standards ("IFRS"). The exemptive relief order applies to the preparation of the Company's annual financial statements for years ending on or after January 1, 2010 and interim financial statements for interim periods ending on or after the completion of the Qualifying Transaction (as hereafter defined). Accordingly, the financial information contained in this MD&A has been prepared in accordance with IFRS and in accordance with International Accounting Standard 34 Interim Financial Reporting.

In this 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 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 MD&A are in Canadian dollars.

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

FORWARD-LOOKING STATEMENTS

Certain statements in this MD&A may constitute "forward-looking statements". Forward-looking statements are statements that address or discuss activities, events or developments that the Company expects or anticipates may occur in the future. When used in this MD&A, words such as "estimates", "expects", "plans", "anticipates", "projects", "will", "believes", "should", "could", "may" and other similar terminology are intended to identify such forward-looking statements. Forward-looking statements reflect the current expectations and beliefs of the Company's management. Because forward-looking statements involve known and unknown risks, uncertainties and other factors, actual results, performance or achievements of the Company or industry may be materially different from those implied by such forward-looking statements.

Forward-looking statements involves significant uncertainties, should not be read as a guarantee of future performance or results, and will not necessarily be an accurate indication of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including those matters described in Schedule "A" to the filing statement of the Company dated May 25, 2010 under the heading "Risk Factors", available on SEDAR at www.sedar.com. Accordingly, readers should exercise caution in relying upon forward-looking statements and the Company undertakes no obligation to publicly revise them to reflect subsequent events or circumstances, except as required by law.

COMPLETION OF QUALIFYING TRANSACTION

On June 3, 2010, Conifex, formerly West Fourth Capital Inc. ("**Fourth**"), completed its qualifying transaction (the "**Qualifying Transaction**") with DTR Wood Acquisitionco Ltd. ("**DTR**") as a plan of arrangement (the "**Arrangement**") pursuant to the provisions of the *Business Corporations Act* (British Columbia). Pursuant to the Arrangement, Conifex acquired all of the issued and outstanding securities of DTR in exchange for securities of Conifex. The Arrangement was a qualifying transaction for Conifex, formerly a capital pool company, under the policies of the TSX Venture Exchange. In connection with the Arrangement, Fourth changed its name to "Conifex Timber Inc.". On June 8, 2010, the Company's common shares began trading on the TSX Venture Exchange under the new trading symbol "CFF".

The acquisition of the securities of DTR was accounted for as a reverse asset acquisition. Accordingly, the Company's consolidated interim financial statements incorporate the financial statements of the Company and its wholly-owned subsidiaries from the date of completion of the Qualifying Transaction. The comparative amounts included in the interim consolidated financial statements are those of DTR. DTR, incorporated on October 22, 2004, was formed for the purpose of investing in the forest industry in the interior region of British Columbia and elsewhere in Canada.

OTHER SIGNIFICANT EVENTS

On June 3, 2010, the Company completed the acquisition (the "**Mackenzie Acquisition**") of certain assets (the "**Mackenzie Assets**") located in Mackenzie, British Columbia. The Mackenzie Assets included two sawmill complexes, harvesting rights to 932,500 cubic metres of sawlogs annually, power generation assets and a paper mill (excluding the headbox) that is being held for sale. In connection with the Mackenzie Acquisition, DTR completed a private placement (the "**Private Placement**") consisting of the sale of 10,787,878 subscription receipts at a price of \$8.25 per subscription receipt for gross proceeds of approximately \$89 million. Each subscription receipt was, pursuant to the Arrangement, exchanged for DTR common shares from treasury on a one-to-one basis, without further payment or consideration, in connection with the Qualifying Transaction.

The Company has committed approximately \$30 million to a capital expenditure program (the "**Cap-Ex Program**") at its Fort St. James manufacturing facility. The purpose of the program is to upgrade and modernize specific converting and finishing processes to enable cost effective operations on a two-shift basis.

In connection with the Qualifying Transaction, the Company changed its fiscal year end to December 31. Prior to the Qualifying Transaction, DTR's fiscal year end was the 52 or 53

weeks ending the last Saturday of December and customarily consisted of four 13-week quarters, with every sixth year including 53 weeks.

SELECTED ANNUAL INFORMATION

The following table sets forth selected financial data derived from the Company's annual audited financial statements for the fiscal year ended December 26, 2009:

Year ended December 26	2009
(\$000's except per share information)	
Revenues*	31,333
Expenses	42,281
Operating loss	(10,948)
Net loss	(10,331)
Basic and diluted loss per share	(2.45)

* Revenues reflect shipments for the nine-month period commencing April 2009.

As at December 26, 2009, the Company had total assets of \$27,336,000.

The Company did not commence commercial operations until the first quarter of 2009 and did not deliver its first shipment of lumber until the second quarter of 2009. Accordingly, prior period information has not been presented above as management believes it is of little assistance to readers.

REVIEW OF OPERATING RESULTS

Overview

Prior to the acquisition of the Mackenzie Assets, the Company's operating rate was approximately 50% based on the operation of one shift at the Fort St. James sawmill. Subsequent to the Mackenzie Acquisition, the operating rate has been approximately 22% when full production capacity is calculated on an annualized two-shift basis at all three sawmills. A specific start-up date at the Mackenzie site has not been determined. The Company currently absorbs the significant fixed costs related to its timberlands and manufacturing operations that would be required to operate the mills at full capacity.

The first phase of the Company's Cap-Ex Program was completed in May 2010 and entailed the shutdown of the main Fort St. James planer mill for a three week period commencing on April 16, 2010. The curtailment of the finishing operations adversely impacted the Company's financial results for the quarter ended June 30, 2010. The volume of lumber shipped during this quarter was 12% lower than recent quarterly shipment averages; overall planer efficiency was reduced and unit manufacturing costs increased by 8% over recent average levels. Although it is difficult to quantify the financial impact of the planned shutdown of the Fort St. James planer mill, the shutdown occurred during a period when lumber prices reached their highest 2010 year-to-date levels, and a level not achieved since 2006.

Prices¹ for WSPF 2x4 #2 & Btr (“WSPF”) began the six-month period ended June 30, 2010 at US\$208, peaked at US\$320 in late April, bottomed at US\$188 the week of June 21st and closed out the period virtually unchanged at US\$206. The increase in prices earlier in the year was driven by curtailed supply and demand side factors such as low inventories in the supply chain, modest improvement in the housing market and tax credit incentives in the U.S. related to home purchases. A combination of increased production, replenished inventories and weaker demand reversed the price gains of the earlier period.

The higher WSPF prices in the earlier months of 2010 resulted in a reduction in the export tax rate charged on lumber shipments from British Columbia to the U.S. from 15% in prior periods to 10% in May and to a zero rate in June.

During the second quarter of 2010, the Canadian dollar traded between \$0.93 to \$1 US and averaged \$0.97 US. During the second quarter of 2009, the Canadian dollar traded between \$0.79 to \$0.92 US and averaged \$0.86 US².

KEY OPERATING RESULTS

(millions of dollars)	Q2-10	Q1-10	YTD-10	Q2-09	YTD-09
Revenues	\$ 12.6	\$ 12.1	\$ 24.7	\$ 8.4	\$ 8.6
Net loss	\$ (2.4)	\$ (1.6)	\$ (4.0)	\$ (1.7)	\$ (7.1)
EBITDA*	\$ (0.9)	\$ (0.9)	\$ (1.8)	\$ (1.1)	\$ (6.4)
 (millions of fbm)					
Shipments	30.7	32.8	63.5	28.0	28.0
Production	41.3	39.5	80.8	36.0	45.0

* 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 the Company's management to evaluate the Company's performance. As EBITDA is a non-GAAP measure, it may not be comparable to EBITDA 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.

The Company recorded a net loss of \$2.4 million or \$0.31 per share for the second quarter of 2010 and a net loss of \$4.0 million or \$0.67 per share for the six month period ended June 30, 2010. This compares to a net loss of \$1.7 million or \$0.40 per share for the second quarter of 2009 and net loss of \$7.1 million or \$1.71 per share for the six months ended June 30, 2009.

EBITDA was (\$0.9) million for the second quarter of 2010 and (\$1.8) million for the six month period ended June 30, 2010. EBITDA was (\$1.1) million for the second quarter of 2009 and (\$6.4) million for the six months ended June 30, 2009.

In connection with the Arrangement, the Company completed the Private Placement for net proceeds of \$85.9 million. Part of the proceeds was used to acquire the Mackenzie Assets. The Company drew down \$2.3 million of a previously approved credit facility during the second quarter of 2010 and had cash on hand of \$52 million at the end of the second quarter.

¹ Prices as quoted in Random Lengths Publications Inc.

² Bank of Canada website www.bankofcanada.ca

Production and Sales

The Company commenced operating one shift at its Fort St. James sawmill in March 2009 with shipments beginning in April 2009. While monthly lumber production has averaged 12.4 million board feet since start-up, monthly production averaged 11% greater than this during the most recent quarter. Despite the higher lumber production, monthly lumber shipments in the second quarter were 12% below the average of 11.6 million board feet achieved since start-up. Although a portion of the lower shipments were due to temporarily reduced shipment volumes to China, the main contributor was the Cap-Ex Program that required the shutdown of the main Fort St. James planer mill for three weeks commencing on April 16, 2010. Shipments in the second quarter of 2009 were 20% lower than average quarterly shipments as the Company was accumulating an appropriate inventory mix during the start-up period.

Revenues from the second quarter of 2010 increased by \$4.2 million compared to the second quarter of 2009 due to a 9% increase in shipment volume and a 33% increase in unit sales price. WSPF prices averaged \$273 during the second quarter of 2010 compared to \$203 during the second quarter of 2009. Revenues from sales of by-products contributed 16% to total revenue during the second quarter of 2010 (13.5% year-to-date) and is similar to percentages achieved for the same periods in the previous year. Total revenues were \$24.7 million for the six months ended June 30, 2010 compared to \$8.6 million for the six months ended June 30, 2009. The increase in shipments for the current year is attributable to higher lumber prices and to increased shipment volumes as the Fort St. James sawmill did not commence lumber shipments until early April of 2009.

Operations

The Company completed the first phase of its Cap-Ex Program to upgrade and modernize its planing and finishing facilities at the Fort St. James mill in May 2010. A key component of this phase involved the installation of a GradExpert Automated Grading system which required a three week shutdown of the main Fort St. James planer mill.

The installation was completed as scheduled and the planer mill resumed operations in May 2010. The GradExpert system is designed to grade kiln-dried, surfaced spruce, pine and fir, commonly referred to as "SPF", lumber pieces with a minimum of human intervention. The system requires an initial testing phase during which information regarding defect tolerances for specific grades is collected and refined. The operators used tighter than typical grade tolerances during the testing phase in an effort to ensure customers of the mill do not receive below grade quality lumber. This resulted in the production of a higher than average outturn of lower grade products during this period. Now that the testing phase is complete, the GradExpert system is contributing to increased planer efficiency and throughput, improved grade outturns, decreased trim loss, and reduced manning costs. The GradExpert system also provides the potential to broaden the range of products manufactured at the mill.

Cost of goods sold during the second quarter of 2010 was \$3.4 million higher than for the same period in 2009. The revaluation of logs and lumber inventory to net realizable value ("NRV") increased cost of goods sold for the second quarter of 2010 by \$0.8 million and decreased cost of goods sold by \$0.9 million for the second quarter of 2009. Lower planer efficiency rates increased unit manufacturing costs during the second quarter of 2010. Cost of goods sold for the six months ended June 30, 2010 was \$19.2 million compared to \$11.8 million for the six months ended June 30, 2009. The higher per unit costs for the six months ended June 30,

2009 are attributable to lower operating rates and an inventory valuation adjustment to NRV of \$2.1 million compared to an adjustment of \$0.3 million for the six months ended June 30, 2010.

Freight and distribution costs vary with shipment volumes for each period and per unit costs remain stable. Export tax amounts are determined by applying the prescribed export tax rate to the freight-on-board mill value of softwood lumber shipments to the United States. The export tax rate averaged 8.3% during the second quarter of 2010 compared to 15% throughout all prior periods. During the second quarter of 2010, approximately 40% of the Company's total volume was shipped to the U.S. compared to 50% during the second quarter of 2009. The remaining volume was shipped to customers in Canada, China and Japan.

Selling, general and administrative expenses increased by \$0.6 million for the second quarter of 2010 over the second quarter of 2009, and \$1.2 million for the six month period ended June 30, 2010 over the six month period ended June 30, 2009. The increases for both time periods are generally attributable to variable shipping costs associated with the higher volume of shipments, fixed expenses related to the acquisition of the Mackenzie Assets and the addition of a corporate office in Vancouver, British Columbia in June 2010

Other Income and Expense

Significant items included in other income and expense for the second quarter of 2010 include non-cash charges for accretion of convertible debenture of \$0.5 million and revaluation of Fourth shares to fair value of \$0.5 million. A gain of \$0.3 million from lumber price derivatives was recorded in the second quarter of 2010 compared to a loss of \$0.1 million in the second quarter of 2009.

CASH FLOW AND LIQUIDITY

SELECTED CASH FLOW ITEMS

(millions of dollars)	Q2-10	Q1-10	YTD-10	Q2-09	YTD-09
Operating Activities					
Cash used before working capital changes	(0.5)	(1.1)	(1.6)	(2.2)	(4.5)
Non - cash working capital change	(0.7)	(2.7)	(3.4)	-	(6.0)
Cash used in operating activities	(1.2)	(3.8)	(5.0)	(2.2)	(10.5)
Investing Activities					
Additions to property, plant, equipment	(2.4)	(2.4)	(4.8)	(0.2)	(0.7)
Acquisition of Mackenzie assets	(34.5)	-	(34.5)	-	-
Other	0.2	(0.2)	-	(0.1)	(0.3)
Cash used in investing activities	(36.7)	(2.6)	(39.3)	(0.3)	(1.0)
Financing Activities					
Proceeds from loans	2.3	-	2.3	0.7	0.7
Proceeds from convertible notes	-	2.0	2.0	-	-
Proceeds from issue of share capital	85.9	-	85.9	1.0	1.0
Cash provided from financing activity	88.2	2.0	90.2	1.7	1.7
Change in cash	50.3	(4.4)	45.9	(0.8)	(9.8)

The Company's principal sources of funds are cash flow from operations, cash on hand and its available credit facility related to the Cap-Ex Program at the Fort St. James Mill. The Company's principal uses of funds consist of operating and capital expenditures.

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 maintenance downtime, 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 ensure adequate supply of fibre to its mills during the spring months. Changes in sales volume can affect the level of receivables and influence overall working capital levels. The Company believes its management practices with respect to working capital conform to common industry practices.

Operating activities consumed cash of \$5 million during the first six months of 2010 compared to \$10.5 million during the first six months of 2009. The higher cash usage during the first six months of 2009 is attributable to a larger operating loss before working capital changes and the increase in working capital required to commence operations at the Fort St. James site.

Investing activities in the first six months of 2010 included the acquisition of the Mackenzie Assets and completion of the first phase of the Cap-Ex Program at Fort St. James. Of the total \$6.2 million committed to this phase, \$1 million was paid during the last quarter of 2009, \$4.8 million was paid during the first six months of 2010 and the balance will be paid in subsequent period(s).

Financing activities provided cash of \$88.2 million during the second quarter of 2010 and \$2 million during the second quarter of 2009. In connection with the Mackenzie Acquisition, the Company completed the Private Placement for net proceeds of \$85.9 million (gross proceeds of \$89 million less \$3.1 million in costs of issue).

In August 2009, the Company obtained a \$8.5 million loan facility related to the Cap-Ex Program at Fort St. James. The loan is being provided as part of the Community Adjustment Fund ("CAF") loan program sponsored by the Northern Development Initiative Trust. The CAF loan carries a fixed interest rate of 3.75% repayable in quarterly instalments over a five year period commencing June 1, 2011. The Company drew down \$2.3 million of this credit facility during the second quarter of 2010.

At the end of the second quarter, the Company had cash on hand of \$52 million.

Changes in Equity

Sources of contributions to equity during the second quarter of 2010 included net proceeds of \$85.9 million from the Private Placement, net adjustment of \$0.4 million related to the Qualifying Transaction, contributed surplus of \$0.1 from the Company's share based compensation plan and a minimal amount from the exercise of stock options. The additions to equity were offset by a net loss of \$2.4 million for a net change to equity of \$84 million during the period.

SELECTED QUARTERLY FINANCIAL INFORMATION

Quarterly Earnings Summary	2010			2009			2008	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
(millions of dollars except share and per share amounts)								
Sales -Lumber	10.6	10.8	9.6	10.7	7.3	-	-	-
- By-products	2.0	1.3	1.2	1.2	1.1	0.2		
Total Sales	12.6	12.1	10.8	11.9	8.4	0.2	-	-
Operating loss	(1.8)	(1.0)	(2.4)	(1.0)	(1.9)	(5.4)	(2.7)	(0.7)
Net earnings (loss)	(2.4)	(1.6)	(2.1)	(0.9)	(1.7)	(5.4)	(2.5)	(1.8)
Net earnings (loss) per share - basic and diluted	(0.31)	(0.39)	(0.49)	(0.21)	(0.40)	(1.31)	(0.61)	(0.79)
EBITDA	(0.9)	(0.9)	(1.5)	(0.3)	(1.1)	(5.3)	(2.7)	(2.0)
Shares outstanding - end of period (millions)	15.1	4.3	4.3	4.3	4.3	4.1	4.1	4.1
Shares outstanding - weighted average (millions)	7.6	4.3	4.3	4.3	4.2	4.1	4.1	2.3
Statistics								
Lumber shipments (MMfbm)	30.7	32.8	36.2	39.3	28.0	-	-	-
Average exchange rate - US\$/Cdn\$	0.973	0.961	0.947	0.912	0.858	0.803	0.825	0.960
Average WSPF 2x4 #2&Btr lumber price (US\$)	\$266	\$268	\$205	\$191	\$174	\$155	\$190	\$263
Average WSPF 2x4 #2&Btr lumber price (Cdn\$)	\$273	\$279	\$216	\$209	\$203	\$193	\$230	\$274

Reconciliation of EBITDA to Net Loss	2010			2009			2008	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
(millions of dollars)								
Net earnings (loss)	(2.4)	(1.6)	(2.1)	(0.9)	(1.7)	(5.4)	(2.5)	(1.8)
Add: Interest (income) expense							(0.2)	(0.1)
Depreciation and amortization	0.5	0.5	0.3	0.3	0.3	0.1	0.0	0.0
Deferred union payroll liability		0.2	0.2	0.2	0.2			
Share based compensation	0.1	0.1	0.1	0.1	0.1	0.1		
Accretion of convertible debentures	0.5							
Revaluation of Fourth shares to fair value	0.5							
EBITDA*	(0.9)	(0.9)	(1.5)	(0.3)	(1.1)	(5.3)	(2.7)	(2.0)

*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, price fluctuations in commodities associated with revenue derived from by-products and movements 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.

ACQUISITION OF MACKENZIE ASSETS

On March 24, 2010, the Company and Abitibi-Consolidated Company of Canada ("Abitibi") entered into an Asset Purchase Agreement (the "APA"), as amended, for the acquisition of certain sawmill and other assets located at Mackenzie, British Columbia. The Company

completed the acquisition on June 3, 2010. Total consideration paid included cash of \$33.5 million plus an amount for net working capital and assumed liabilities.

The Mackenzie Assets include two sawmills, including planer mills, with a combined annual production capacity of 445 million board feet of lumber on a two-shift basis, a forest licence in the Mackenzie timber supply area with an allowable annual cut of approximately 932,500 cubic metres, a steam/power plant and associated turbine and boiler, and a paper mill (excluding the headbox). The Company intends to dispose of the paper mill assets but will retain the power generation assets. The Company assumed certain liabilities of Abitibi including reforestation, environmental and certain employee related liabilities.

The Mackenzie Assets have generally not been operated by Abitibi on a continuous basis since December 2007 due to market conditions, but the sawmills and planer mills were kept in operating and start-up condition. Portions of the assets were operated on an interim basis in the late fall of 2009 and first quarter of 2010.

The purchase of the Mackenzie Assets is consistent with the Company's long term business strategy to locate sawmilling and forestry operations in promising fibre supply regions and to build a margin-focused lumber business of sufficient size and scale to compete successfully with the best mills in North America.

The Mackenzie Acquisition was financed through the completion of the Private Placement for gross proceeds of approximately \$89 million.

The purchase price of the Mackenzie Assets and related transaction costs have been allocated on a preliminary basis to the fair value of the assets acquired and related liabilities arising from the transaction based on agreed upon values in the APA and on management's best estimates and taking into account all available information to June 30, 2010. The purchase price allocation is preliminary and subject to adjustment in accordance with further refinement of fair value allocations.

A specific start-up date at this site has not been determined as negotiations on certain agreements need to progress further before the scope and extent of the start-up can be determined.

COMPLETION OF PRIVATE PLACEMENT

In connection with the Arrangement, the Company completed the Private Placement for gross proceeds of approximately \$89 million. The Private Placement consisted of the sale of subscription receipts that were subsequently exchanged for common shares of DTR from treasury. In addition to the purchase of the Mackenzie Assets, the Company intends to use the funds from the financing to support the Cap-Ex Program, working capital and for general corporate purposes.

CAPITAL EXPENDITURE PROGRAM AT FORT ST. JAMES MILL

The Company has approved the Cap-Ex Program in the amount of \$30 million for its manufacturing complex at Fort St. James. Conifex purchased the Fort St. James Assets in August 2008. The sawmill had been idled by its previous owner in September 2007 due to market conditions and only a nominal amount had been invested in the facility in recent years.

The main focus of the Cap-Ex Program will be achieving a better balance between the sawmilling and planing capacity and strengthening lumber grading capabilities. As the site is presently constituted, it is not economically feasible to operate two shifts because of planer speed limitations.

The first phase of the Cap-Ex Program was completed in the second quarter of 2010 at a cost of approximately \$6 million and involved the installation of an automated grading system. The second phase will cost approximately \$24 million and is expected to be completed by the end of 2010 with minimal disruptions to the current one shift operations. Projects to be completed during the second phase will increase the productivity of the planer to match sawmill production, increase lumber drying capacity and improve lumber drying quality, and increase log throughput at the sawmill. Benefits upon completion of the various projects include reduced labour and fuel costs, increased lumber revenue through improved grade outturns and increased recoveries, and increased by-product revenue through improved quality.

The Cap-Ex Program will be funded by a combination of a \$8.5 million Community Access Fund loan sponsored by the Northern Development Initiative Trust (NDIT), training and capital improvement grants from the NDIT, and cash reserves on hand.

OUTSTANDING SECURITIES

As at the date hereof, the Company had 15,136,858 issued and outstanding common shares, 244,114 long-term incentive plan awards issued under the Company's long-term incentive plan dated June 3, 2010, and stepped rate subordinated convertible promissory notes in the aggregate principal amount of \$10,000,000, which notes are convertible into a maximum of 1,250,000 common shares of the Company, excluding any common shares issuable in payment of accrued interest thereon.

ACCOUNTING POLICY CHANGES

Operating Segments

Effective December 28, 2009, the Company adopted a new accounting standard (IFRS 8 *Operating Segments*) that was issued by the International Accounting Standards Board ("**IASB**"). IFRS 8 was revised and now requires disclosure of information about segment assets. This accounting policy change was adopted on a prospective basis with no restatement of prior period financial statements.

Revised IAS 23, *Borrowing Costs*, is effective for the year ended December 31, 2010. IAS 23 removes the option to expense borrowing costs and requires an entity to capitalize borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. The adoption of this standard did not have a material impact on the financial statements.

Amendment IAS 39, *Financial Instruments - Recognition and Measurement*, is effective for the year ended December 31, 2010. The application of this standard amends the principles that affect a hedged risk. The adoption of this standard did not have a material impact on the financial statements.

Amendment IFRS 7, *Financial Instrument Disclosures*, is effective for the year ended December 31, 2010. The application of this revised standard impacts the presentation and format of the primary statements and notes and these disclosures have been revised accordingly in the 2010 financial statements.

The following standards have been issued but are not yet effective:

		Effective for annual periods beginning on or after
IAS 24	(Revisions) Related party disclosures – which clarifies the definition of a related party	January 1, 2011
IFRS 9	(New standard) Financial Instruments – which introduces certain new requirements for the classification and measurement of financial assets	January 1, 2013
IFRIC 19	New Interpretation Accounting for situations where financial liabilities are settled using equity instruments	July 1, 2010

A detailed analysis of the possible applicability and potential effect of the pronouncements included above has not yet been performed.

The significant accounting policies adopted in these financial statements are set out in Note 2 of the interim consolidated financial statements.

OUTLOOK

Recovery in the U.S. housing market is expected to remain constrained by the projected high rate of foreclosures, weaker employment numbers and cautious credit markets. Demand for lumber products in the North American markets is expected to mirror typical seasonal and cyclical industry patterns for the balance of the year in the absence of significant supply or demand side shocks. Seasonal building activity is expected to sustain demand for the duration of the third quarter and prices are expected to remain relatively stable. The reduction of inventory replenishment in anticipation of seasonal slowdowns is expected to reduce demand and prices over the winter months. It is possible that production curtailments taken in response to lower prices coupled with thin inventories in the supply chain could lead to increased price volatility in response to even slight changes in demand.

ADDITIONAL INFORMATION

Additional information about the Company is available on SEDAR at www.sedar.com.