



CONIFEX

**CONIFEX TIMBER INC.  
SECOND QUARTER 2021**

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

**August 10, 2021**

*This Management's Discussion and Analysis ("MD&A") provides a review of the financial condition and results of operations of Conifex Timber Inc. ("Conifex", "us", "we", or "our"), on a consolidated basis, for the quarter ended June 30, 2021 relative to the quarters ended March 31, 2021 and June 30, 2020. This interim MD&A should be read together with our unaudited condensed consolidated interim financial statements for the quarters ended June 30, 2021 and 2020, and our 2020 annual MD&A and our December 31, 2020 audited consolidated financial statements and notes thereon, which have been prepared in accordance with International Financial Reporting Standards ("IFRS") and filed on SEDAR at [www.sedar.com](http://www.sedar.com).*

*In this MD&A, reference is made to "EBITDA" and "adjusted EBITDA". EBITDA represents earnings before finance costs, taxes, depreciation and amortization. Adjusted EBITDA is calculated to exclude unusual items that are not ongoing and do not reflect our ongoing operations. Adjusted EBITDA excludes foreign exchange translation gains or losses on long-term debt, restructuring costs, proceeds from insurance claims and gains or losses on sale of assets. We disclose EBITDA and adjusted EBITDA as it is a measure used by analysts and by our management to evaluate our performance. As EBITDA and adjusted EBITDA are not generally accepted earnings measures under IFRS, and neither has a standardized meaning prescribed by IFRS, they may not be comparable to EBITDA and adjusted EBITDA calculated by other companies. In addition, EBITDA and adjusted EBITDA are not substitutes for net earnings or cash flow, as determined in accordance with IFRS, and therefore readers should consider those measures in evaluating our performance.*

*In February 2020, we sold our US Sawmill Business (as defined herein). In accordance with IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, the operating results previously reported for the US Sawmill Business were restated as discontinued operations for the relevant periods and separated from our continuing operations. Unless otherwise indicated, our discussion and analysis herein reflects our continuing operations. In accordance with IFRS 8, Operating Segments, we also combined our previous reporting segments, including our lumber and bioenergy operating segments, into a single reportable segment. Accordingly, all previously segmented information has been restated to conform to the current presentation for all periods presented. For further information, refer to Note 6 to our consolidated financial statements for the years ended December 31, 2020 and 2019.*

*In this interim MD&A, all references to "\$" are to Canadian dollars and references to "US\$" are to United States dollars.*

**Forward-Looking Statements**

*This interim MD&A contains certain forward-looking information that reflects our current views and/or expectations with respect to our beliefs, assumptions, estimates and forecasts about our business and the industries and markets in which we operate. 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: the realization of expected benefits of completed, current and any contemplated capital projects and the expected timing and budgets for such projects; the growth and future prospects of our business, including the impact of COVID-19 thereon; our expectations regarding our results of operations and performance; our planned operating format and expected operating rates; our perception of the industries or markets in which we operate and anticipated trends in such markets and in the countries in which we do business; our ability to supply our manufacturing operations with wood fibre and our expected cost for wood fibre; our expectation for market volatility associated with, among other things, the softwood lumber dispute with the U.S.; that we could be negatively impacted by the duties or other protective measures on our products, such as antidumping duties or countervailing duties on softwood lumber; continued positive relations with Aboriginal groups; the development of a longer-term capital plan and the expected benefits therefrom; demand and prices for our products; our ability to develop new revenue streams; the availability and use of credit facilities or proceeds therefrom; and future capital expenditures.*

*Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking statements may include, but are not limited to, our future debt levels; that we will complete our projects in the expected timeframes and as budgeted; that we will effectively market our products; that capital expenditure levels will be consistent with those estimated by our management; that the US housing market will continue to improve; that there will be no unforeseen disruptions affecting the operation of our power generation plant and that we will be able to continue to deliver power therefrom; our ability to obtain financing on acceptable terms, or at all; that interest and foreign exchange rates will not vary materially from current levels; the general health of the capital markets and the lumber industry; and the general stability of the economic environments within the countries in which we operate or do business.*

*Persons reading this interim MD&A are cautioned that statements comprising forward-looking information are only predictions, and that our 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 similar 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 2020 annual MD&A dated March 2, 2021 available on SEDAR at [www.sedar.com](http://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. Conifex does not undertake any obligation to update any forward-looking information, except as required by applicable securities laws.*

## **RECENT DEVELOPMENTS**

### ***Normal Course Issuer Bid***

In December 2020, we commenced a normal course issuer bid ("**NCIB**") for our common shares. Under the NCIB, we may purchase up to a maximum of 2,944,320 of our outstanding common shares. Pursuant to the NCIB, we may not repurchase more than (i) \$5.0 million of our common shares between the period of November 30, 2020 and September 30, 2021 and (ii) \$5.0 million of our common shares between the period of October 1, 2021 and the expiry of the bid (the "**NCIB Limitations**"). Any common shares acquired under the NCIB will be purchased at the market price up to a daily maximum of 12,500 common shares, being 25% of the average daily trading volume for the six months prior to the bid, subject to the block purchase exemption. All common shares acquired by us under the NCIB will be cancelled following purchase. The NCIB will terminate on November 30, 2021 or earlier if we have completed our purchases of the securities subject to the NCIB or if we otherwise determine that it is appropriate to suspend or terminate the bid. In the three month period ended June 30, 2021, we purchased and cancelled 1,457,000 shares under the NCIB, for a total of 2,379,800 shares purchased and cancelled since the inception of the NCIB.

Subsequent to the period end, we amended our \$10.0 million secured revolving credit facility with Wells Fargo Capital Finance Corporation Canada (the “**Revolving Credit Facility**”) to revise the NCIB Limitations so that we may repurchase not more than (i) \$7.0 million of our common shares between the period of November 30, 2020 and September 30, 2021 and (ii) \$9.0 million of our common shares between the period of October 1, 2021 and September 30, 2022.

## SUMMARY

Continuing operations for the comparative periods discussed in this MD&A primarily comprise operating results from our Mackenzie sawmill, our power plant and, as applicable, our previously sold sawmill in Fort St. James, British Columbia (“BC”), which was largely curtailed in May 2019 and sold in November 2019.

Operating and financial results in 2020 were materially impacted by the curtailment of our Mackenzie sawmill from April 6 to July 6, 2020.

### Selected Financial Information<sup>(1)</sup>

(unaudited, in millions of dollars, except earnings per share and share information)	Q2 2021	Q1 2021	YTD 2021	Q2 2020	YTD 2020
<b>Sales</b>					
Lumber – Conifex produced	80.1	39.9	120.0	4.7	25.6
Lumber – wholesale	9.0	0.6	9.6	1.2	1.2
By-products	2.7	2.4	5.1	0.2	1.9
Bioenergy	4.7	3.7	8.4	4.7	12.7
	96.5	46.6	143.1	10.8	41.4
Operating income (loss)	33.5	8.7	42.2	(1.4)	(8.2)
EBITDA from continuing operations <sup>(2)</sup>	37.8	9.7	47.5	(1.2)	(4.7)
Net income (loss) from continuing operations	26.1	4.5	30.6	(2.7)	(10.9)
Net income (loss) from discontinued operations	-	-	-	(0.3)	0.2
<b>Net income (loss)</b>	26.1	4.5	30.6	(3.0)	(10.7)
<b>Basic and diluted earnings (loss) per share</b>					
Continuing operations	0.56	0.10	0.66	(0.05)	(0.23)
Discontinued operations	-	-	-	(0.01)	-
Total basic and diluted earnings (loss) per share	0.56	0.10	0.66	(0.06)	(0.23)
Shares outstanding – weighted average (millions)	46.3	46.4	46.2	46.9	46.9
<b>Reconciliation of EBITDA to net income (loss)</b>					
Net income (loss) from continuing operations	26.1	4.5	30.6	(2.7)	(10.9)
Add: Finance costs	1.1	1.1	2.3	1.2	4.7
Amortization	2.1	2.2	4.2	1.1	4.0
Deferred income tax expense (recovery)	8.5	1.9	10.4	(0.8)	(2.5)
EBITDA from continuing operations <sup>(2)</sup>	37.8	9.7	47.5	(1.2)	(4.7)

### Selected Operating Information

Production – WSPF lumber (MMfbm) <sup>(3)</sup>	49.0	51.0	100.0	2.4	40.6
Shipments – WSPF lumber (MMfbm) <sup>(3)</sup>	55.5	37.8	93.3	8.5	46.1
Shipments – wholesale lumber (MMfbm) <sup>(3)</sup>	5.8	0.7	6.5	1.6	1.6
Electricity production (GWh)	50.9	25.0	75.9	51.2	106.0
Average exchange rate – \$/US\$ <sup>(4)</sup>	0.814	0.790	0.802	0.722	0.733
Average WSPF 2x4 #2 & Btr lumber price (US\$) <sup>(5)</sup>	\$1,290	\$982	\$1,136	\$357	\$378
Average WSPF 2x4 #2 & Btr lumber price (\$) <sup>(6)</sup>	\$1,584	\$1,244	\$1,414	\$494	\$515

(1) Reflects results of continuing operations, except where otherwise noted.

(2) Conifex’s EBITDA calculation represents earnings before finance costs, taxes, and depreciation and amortization.

(3) MMfbm represents million board feet.

(4) Bank of Canada, [www.bankofcanada.ca](http://www.bankofcanada.ca).

(5) Random Lengths Publications Inc.

(6) Average SPF 2x4 #2 & Btr lumber prices (US\$) divided by average exchange rate.

## REVIEW OF SECOND QUARTER 2021 FINANCIAL RESULTS

During the second quarter of 2021, we recognized net income from continuing operations of \$26.1 million, or \$0.56 per share compared to \$4.5 million or \$0.10 per share in the previous quarter and a net loss of \$3.0 million or \$0.06 per share in the second quarter of 2020.

North American lumber market prices climbed considerably through most of the quarter, reaching a record high of US\$1,630 in May 2021. In June, market prices began a continued slide from the historically elevated levels driven by a slowdown in North American repair and remodelling activities and elevated lumber inventory supply in the market. US housing starts on a seasonally adjusted annual basis averaged 1,550,000 in the second quarter of 2021, down 4% from the previous quarter and up 44% from the second quarter of 2020. During the quarter, home construction activity for the single-family housing market remained strong, while multi-family housing starts declined. Lumber consumption per unit in single-family housing starts is generally considered to be two to three times greater than in multi-family housing starts.

The US dollar averaged US\$0.814 for each Canadian dollar during the second quarter of 2021, a level which represented a strengthening of the Canadian dollar over the previous quarter<sup>1</sup>. Canadian dollar-denominated benchmark Western Spruce/Pine/Fir (“WSPF”) prices, which averaged \$1,584 in the second quarter of 2021, increased by 27% or \$340 from the previous quarter and by 221% or \$1,090 from the second quarter of 2020. The sustained lumber demand, coupled with the impact of supply disruptions caused by railcar supply challenges, resulted in an overall increase to the benchmark WSPF lumber price during the quarter.

### ***Lumber Operations***

Our lumber production in the second quarter of 2021 totalled approximately 49.0 million board feet, representing operating rates of approximately 82% of annualized capacity. In the previous quarter, 51.0 million board feet of lumber was produced. The decrease in lumber production for the second quarter primarily reflected challenging logging conditions characterized by unseasonal wet weather through the quarter, combined with high wildfire risk in the last two weeks of the quarter. The wildfires in the BC interior and the related provincial state of emergency led to a government mandated curtailment of all forest harvesting activities and impacted log availability at our sawmill late in the quarter and through July. In the second quarter of 2020, 2.4 million board feet of lumber was produced due to the curtailment of our Mackenzie sawmill for most of the quarter.

Shipments of Conifex produced lumber totaled 55.5 million board feet in the second quarter of 2021, representing an increase of 47% from the 37.8 million board feet shipped in the previous quarter and an increase of 553% from the 8.5 million board feet of lumber shipped in the second quarter of 2020. As railcar supply challenges eased in the quarter, shipments of Conifex produced lumber increased significantly. Our wholesale lumber program shipped 5.8 million board feet in the second quarter of 2021, representing an increase of 729% from the 0.7 million board feet shipped in the first quarter of 2021 and an increase of 263% from the 1.6 million board feet shipped in the second quarter of 2020.

Revenues from lumber products were \$89.1 million in the first quarter of 2021 representing an increase of 120% from the previous quarter and an increase of 1,410% from the second quarter of 2020. Compared to the previous quarter, the higher revenues in the current quarter were driven by higher shipment volumes and higher realized lumber prices. Decreased revenues during the second quarter of 2020 were primarily the result of the curtailment of our Mackenzie sawmill. Our lumber is typically sold 2-4 weeks in advance of its shipment date, resulting in a lag in our realized lumber prices when compared to concurrent reported lumber prices. As a result, the sharp decline in lumber prices since June 2021 will be realized in the third quarter of 2021.

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<sup>1</sup> Bank of Canada, [www.bankofcanada.ca](http://www.bankofcanada.ca)

Cost of goods sold in the second quarter of 2021 increased by 65% from the previous quarter and increased by 428% from the second quarter of 2020. The increase in cost of goods sold from the prior quarter is due to higher overall shipments in the current quarter, including higher volumes of wholesale shipments, and higher log costs. Unit manufacturing costs remained steady in comparison to the previous quarter and were significantly below the second quarter of 2020 as a result of the curtailment of our sawmill in the prior year.

We expensed countervailing (“**CV**”) and anti-dumping (“**AD**”) duty deposits of \$5.3 million in the second quarter of 2021, \$2.5 million in the previous quarter and \$0.3 million in the second quarter of 2020. The duty deposits were based on a combined rate of 20.23% until December 1, 2020 and 8.99% thereafter. The export taxes during the second quarter of 2021 were significantly greater than the previous quarter due to the higher lumber shipment volumes made to the US market.

### ***Bioenergy Operations***

Our Mackenzie power plant sold 50.9 gigawatt hours of electricity under our Electricity Purchase Agreement (“**EPA**”) with BC Hydro and Power Authority (“**BC Hydro**”) in the second quarter of 2021 representing approximately 90% of targeted operating rates. Our Mackenzie power plant sold 25.0 and 51.2 gigawatt hours of electricity in the previous quarter and second quarter of 2020, respectively. The increase in production in the second quarter of 2021 over the prior quarter is mainly attributable to the successful recommissioning of the power plant on February 21, 2021 following a disruption beginning in December 2020 caused by damage to the plant’s generator. The disruption resulted in 49 days of unplanned downtime during the first quarter of 2021.

We have submitted an insurance claim for physical damage to our equipment and for the loss of revenues from the interruption of operations. We expect to be fully reimbursed for capital expenditures related to the replacement of our generator, subject to deductible amounts, and for lost income for the period covered under our business interruption policy, being the period between the expiry of the waiting period and the recommencement of the power plant. We have recognized \$2.8 million as other income in the second quarter of 2021 to reflect our best estimate of the expected settlement for lost income under our business interruption policy.

Our EPA with BC Hydro, similar to other electricity purchase agreements, provides BC Hydro with the option to “turn down” electricity purchased from us during periods of low demand by issuing a “dispatch order”. In April 2021, BC Hydro issued a dispatch order for 61 days, from May 1 to June 30, 2021. In 2020, our power plant was dispatched for 117 days, from April 24 to August 19, 2020. We continue to be paid revenues under the EPA based upon a reduced rate and on volumes that are generally reflective of contracted amounts. During any dispatch period, we continue to produce electricity to fulfill volume commitments under our Load Displacement Agreement (“**LDA**”) with BC Hydro.

### ***Selling, General and Administrative Costs***

Selling, general and administrative (“**SG&A**”) costs were \$3.0 million in the second quarter of 2021, \$2.2 million in the previous quarter and \$1.9 million in the second quarter of 2020. The higher SG&A costs in the current quarter compared to the previous quarter were primarily attributable to variable compensation costs, including equity-based compensation, and an increased commitment for First Nations and community donations.

### ***Finance Costs and Accretion***

Finance costs and accretion totaled \$1.1 million in the second quarter of 2021, \$1.1 million in the previous quarter and \$1.2 million in the second quarter of 2020. Finance costs and accretion relate primarily to our term loan supporting our bioenergy operations (the “**Power Term Loan**”).

### ***Gain or Loss on Derivative Financial Instruments***

Gains or losses on lumber derivative instruments are recognized as they are settled or as they are marked to market for each reporting period. We entered into lumber futures contracts for downside price protection on a small percentage of our estimated second and third quarter 2021 production. Due to lumber market conditions characterized by rapidly rising prices from April through May 2021, we recorded a loss from lumber derivative instruments of \$0.7 million in the second quarter of 2021. We recorded a loss from lumber derivative instruments of \$0.9 million and \$0.7 million in the previous quarter and in the second quarter of 2020, respectively. The futures contracts were closed and there were no outstanding futures contracts in place as at June 30, 2021.

### ***Foreign Exchange Translation Gain or Loss***

The foreign exchange translation gain or loss recorded for each period on our statement of net income results from the revaluation of US dollar-denominated cash and working capital balances to reflect the change in the value of the Canadian dollar relative to the value of the US dollar. US dollar-denominated monetary assets and liabilities are translated using the period end rate.

The foreign exchange translation impacts arising from the variability in exchange rates at each measurement period on cash and working capital balances resulted in a foreign exchange translation gain of \$0.1 million in the second quarter of 2021, compared to a loss of \$0.3 million in the previous quarter and a loss of \$0.2 million in the second quarter of 2020.

### ***Income Tax***

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities on our balance sheet and the amounts used for income tax purposes. We recorded a deferred income tax expense of \$8.5 million in the second quarter of 2021 and \$1.9 million in the previous quarter, respectively, and a deferred income tax recovery of \$0.8 million in the second quarter of 2020. As at June 30, 2021, we have recognized deferred income tax liability of \$0.6 million.

### ***Discontinued Operations***

In February 2020, we sold our US sawmill business, consisting of our El Dorado, Cross City and Glenwood sawmills and related operations (the "**US Sawmill Business**") for US\$172.8 million, including net working capital of US\$9.8 million. In accordance with IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, the operating results previously reported for the US Sawmill Business were restated as discontinued operations for the relevant periods and separated from our continuing operations.

Net loss from discontinued operations was \$nil in the first and second quarters of 2021, compared to \$0.3 million in the second quarter of 2020.

For further information on discontinued operations, see Note 6 of our consolidated financial statements for the years ended December 31, 2020 and 2019 available on SEDAR at [www.sedar.com](http://www.sedar.com).

## SUMMARY OF FINANCIAL POSITION

(unaudited, in millions of dollars, unless otherwise noted)	<b>Q2</b>	<b>Q4</b>	<b>Q2</b>
	<b>2021</b>	<b>2020</b>	<b>2020</b>
Cash	35.8	11.2	11.5
Cash – restricted	5.6	3.6	6.0
Operating working capital <sup>(1)</sup>	26.1	14.7	6.5
Current portion of revolver and long-term debt	(4.6)	(4.5)	(4.4)
Net current assets	62.9	25.0	19.6
Property, plant and equipment	128.9	130.0	133.4
Other long-term assets	27.9	37.9	40.3
	219.7	192.9	193.3
Non-interesting bearing long-term liabilities	19.3	17.6	18.7
Long-term debt – Power Term Loan	55.5	57.0	58.8
Long-term debt – other <sup>(2)</sup>	1.5	1.9	2.4
Shareholders' equity	143.4	116.4	113.4
	219.7	192.9	193.3
Ratio of current assets to current liabilities	3.2	2.0	1.7
Net debt to capitalization	12%	29%	30%
Net debt to capitalization excluding Power Term Loan	(28%)	(3%)	(8%)

(1) Calculated as the aggregate of trade and other receivables, prepaid expenses and deposits and inventories less the aggregate of trade payables, accrued liabilities and other payables, the current portion of reforestation obligations and employee liabilities.

(2) Consists of leases in 2021 and 2020.

Operating working capital increased by \$11.4 million over the first half of 2021 due primarily to an increase in inventory of \$10.9 million and an increase in trade and other receivables of \$4.8 million, partially offset by an increase in trade payables and employee liabilities. Inventory levels were higher due to a larger volume of log and lumber inventory held at June 30, 2021 compared to December 31, 2020.

Overall debt was \$61.6 million at June 30, 2021 compared to \$63.4 million at December 31, 2020. The reduction of \$1.8 million in debt comprised net lease repayments of \$0.3 million and Power Term Loan payments of \$1.5 million. Our Power Term Loan, which is largely non-recourse to our lumber operations, represents substantially all of our outstanding long-term debt. At June 30, 2021, we had \$58.9 million outstanding on our Power Term Loan, while our remaining long-term debt, consisting of leases, was \$2.7 million.

The ratio of current assets to current liabilities was 3.2:1 at June 30, 2021 compared to 2.0:1 at December 31, 2020 and 1.7:1 at June 30, 2020. The year-over-year change was primarily attributable to an increase in inventory and cash on hand as at June 30, 2021.

As at June 30, 2021, \$102.7 million of our consolidated property, plant and equipment was attributable to our power operations compared to \$103.1 million at December 31, 2020.

We use the net debt to total capitalization ratio to measure our relative debt position and as an indicator of the relative strength and flexibility of our balance sheet. Net debt is calculated as interest-bearing debt less cash. Total capitalization is calculated as the sum of net debt and equity. Net debt at June 30, 2021 decreased by \$28.5 million to \$20.1 million from \$48.6 million at December 31, 2020. The net debt to capitalization ratio was approximately 12% at June 30, 2021, 29% at December 31, 2020 and 30% at June 30, 2020.



## LIQUIDITY AND CAPITAL RESOURCES

### Summary of Cash Flows

(unaudited, in millions of dollars)

	Q2 2021	Q1 2021	YTD 2021	Q2 2020	YTD 2020
<b>Cash generated from (used in)</b>					
Operating activities	35.6	2.0	37.6	1.6	(11.4)
Investing activities	(1.4)	(1.5)	(2.9)	(0.7)	223.5
Financing activities	(4.8)	(5.2)	(10.0)	(1.4)	(200.9)
<b>Increase (decrease) in cash</b>	<b>29.4</b>	<b>(4.7)</b>	<b>24.7</b>	<b>(0.5)</b>	<b>11.2</b>

### Operating Activities

We operate in a cyclical industry. Working capital levels fluctuate throughout the year and are impacted by a variety of factors, including changes in sales volume and prices, shipment patterns, operating rates, seasonality and timing of receivables and payment of payables and expenses. Our fibre inventories exhibit seasonal swings as we increase log inventories during the fall and winter months to help maintain adequate supply of fibre to our Mackenzie sawmill during the spring months. Factors such as disruption of transportation services by third party providers, variability in export shipments and operating rates can impact the level of lumber inventories. We believe our practices with respect to working capital conform to common business practices in our industry.

Operating activities before changes in non-cash working capital generated \$49.2 million of cash in the first half of 2021, compared to net cash usage of \$2.9 million in the first half of 2020. Changes in non-cash working capital used \$11.6 million of cash in the first six months of 2021 and used \$8.5 million in the comparative six month period. The increase in operating cash flows in the first half of 2021 compared to 2020 primarily reflects the positive earnings in the period arising from the market price of lumber, partially offset by the increase in log and lumber inventories.

### Investing Activities

Investing activities utilized cash of \$3.0 million in the first half of 2021 and generated cash of \$223.5 million in the first half of 2020. Investing activities in the first half of 2021 were comprised of investments in property, plant and equipment. Investing activities in the first half of 2020 were comprised primarily of the receipt of \$223.6 million from the sale of our US Sawmill Business.

### Financing Activities

Our financing activities used net cash of \$10.0 million in the first half of 2021 and utilized \$200.9 million in the first half of 2020. Net cash usage in the six month period ended June 30, 2021 was primarily comprised of Power Term Loan payments, payment of finance expenses and purchases of our common shares under the NCIB. In the first half of 2020, financing activities included \$191.8 million to repay in full our previous lumber credit facility and payment of finance expenses of \$7.5 million.

### Liquidity

Our principal sources of funds are cash on hand, cash flows from operations and cash available under our Revolving Credit Facility which was completed in October 2020. The Revolving Credit Facility is available for a term of 3 years and is substantially secured by our lumber inventory, equipment and accounts receivable. The Revolving Credit Facility is undrawn.

Our principal uses of funds consist of operating expenditures, capital expenditures, interest payments and repayment of principal on our Power Term Loan.

At June 30, 2021, we had total liquidity of \$45.8 million, compared to \$21.2 million at December 31, 2020 and \$11.5 million at June 30, 2020. Liquidity at June 30, 2021 was comprised of unrestricted cash of \$35.8 million and unused availability of \$10.0 million under the Revolving Credit Facility.

The increase in our liquidity in the first half of 2021 compared to closing quarter of 2020 was due primarily to the sustained rise in lumber prices, offset partially by the decrease in non-cash working capital driven by escalating log costs at our Mackenzie sawmill and higher overall inventory levels. Compared to the first half of 2020, the increase in our liquidity was largely from the addition of the Revolving Credit Facility and the cash flows generated from operating activities which reflected substantially higher lumber prices year-over-year. Our material contractual obligations remain substantially unchanged from those described in our 2020 annual MD&A and consolidated financial statements for the years ended December 31, 2020 and 2019.

Like other Canadian lumber producers, we were required to begin depositing cash on account of softwood lumber duties imposed by the United States government in April 2017. Cumulative duties of US\$16.3 million paid by us, net of sales of the right to refunds, since the inception of the current trade dispute remain held in trust by the US pending administrative reviews and the conclusion of all appeals of US decisions. We expect future cash flow will continue to be adversely impacted by the CV and AD duty deposits to the extent additional costs on US destined shipments are not mitigated by higher lumber prices.

We monitor our expected liquidity levels and compliance with debt covenants under our Power Term Loan and Revolving Credit Facility by regularly preparing rolling cash flow forecasts to consider upcoming operational requirements, debt service commitments and future business development. Our Power Term Loan also contains certain restrictions on the ability of our power subsidiaries to transfer funds outside of the power entities. We did not have any material commitments for capital expenditures at June 30, 2021. Based on our current level of operations and our present expectations for future periods in light of the existing economic environment, we believe that cash flow from operations, flexibility in levels of investment in operating working capital and availability under our Revolving Credit Facility will be adequate to meet our obligations over the next twelve months.

### ***Off-Balance Sheet Arrangements***

Our off-balance sheet arrangements as at June 30, 2021 were comprised of standby letters of credit totalling \$5.6 million posted by our subsidiary, Conifex Power Limited Partnership. The standby letters of credit are issued to BC Hydro in connection with the EPA and the LDA.

### ***Transactions Between Related Parties***

Other than transactions in the normal course of business with key management personnel, we had no transactions between related parties in the second quarter of 2021 or in the comparative quarters.

## SELECTED QUARTERLY FINANCIAL INFORMATION

### Quarterly Earnings Summary

(unaudited, in millions of dollars, unless otherwise noted)	2021		2020			2019		
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Sales	96.5	46.6	49.8	37.6	10.8	30.6	27.7	22.9
Operating income (loss)	33.5	8.7	4.6	7.0	(1.4)	(6.8)	(11.5)	(8.6)
Net income (loss) from continuing operations	26.1	4.5	2.2	2.0	(2.7)	(8.2)	(10.2)	(11.6)
Net income (loss) – total operations	26.1	4.5	2.3	2.0	(3.0)	(7.7)	(162.6)	(16.6)
Net income (loss) per share – basic and diluted from continuing operations	0.56	0.10	0.05	0.04	(0.05)	(0.18)	(0.22)	(0.25)
Net income (loss) per share – basic and diluted – total operations	0.56	0.10	0.05	0.04	(0.06)	(0.17)	(3.47)	(0.35)
Adjusted EBITDA from continuing operations <sup>(1)</sup>	37.8	9.7	6.8	7.6	(1.1)	0.5	(3.9)	(7.0)
Shares outstanding – weighted average (in millions)	46.3	46.4	47.0	47.0	46.9	46.9	46.9	46.9
<b>Statistics</b> (in millions, except rate and prices)								
Production – WSPF lumber	49.0	51.0	48.3	48.0	2.4	38.2	37.8	26.0
Shipments – WSPF lumber	55.5	37.8	49.1	39.2	8.5	37.6	38.0	34.8
Shipments – wholesale lumber	5.8	0.7	1.8	0.7	1.6	-	-	0.3
Electricity production – GWh	50.9	25.0	41.7	54.9	51.2	54.8	55.1	53.1
Average exchange rate – US\$/ $\text{\$}^{(2)}$	0.814	0.790	0.767	0.751	0.722	0.744	0.758	0.757
Average WSPF 2x4 #2 & Btr lumber price (US $\text{\$}$ ) <sup>(3)</sup>	\$1,290	\$982	\$700	\$768	\$357	\$399	\$380	\$356
Average WSPF 2x4 #2 & Btr lumber price ( $\text{\$}$ ) <sup>(4)</sup>	\$1,584	\$1,244	\$912	\$1,023	\$494	\$536	\$502	\$470
<b>Reconciliation of Adjusted EBITDA to net income (loss)</b>								
Net income (loss) from continuing operations	26.1	4.5	2.2	2.0	(2.7)	(8.2)	(10.2)	(11.6)
Add: Finance costs	1.1	1.1	1.3	1.2	1.2	3.5	21.7	7.0
Amortization	2.1	2.2	2.8	2.9	1.1	2.9	4.8	1.8
Deferred income tax expense (recovery)	8.5	1.9	0.5	1.5	(0.8)	(1.7)	(3.8)	(4.0)
EBITDA <sup>(5)</sup>	37.8	9.7	6.8	7.6	(1.2)	(3.5)	12.5	(6.8)
Add: Foreign exchange (gain) loss on long-term debt	-	-	-	-	-	2.1	(2.4)	2.4
Restructuring costs	-	-	-	-	0.1	1.9	2.6	-
Proceeds from insurance claim	-	-	-	-	-	-	(1.1)	-
Gain on sale of assets	-	-	-	-	-	-	(15.5)	-
Gain on sale of right to duty refunds	-	-	-	-	-	-	-	(2.6)
Adjusted EBITDA from continuing operations	37.8	9.7	6.8	7.6	(1.1)	0.5	(3.9)	(7.0)

(1) Conifex's adjusted EBITDA calculation represents earnings before finance costs, taxes, depreciation and amortization, foreign exchange translation gains or losses on long-term debt, restructuring costs, proceeds from insurance claims and gains or losses on sale of assets.

(2) Bank of Canada, [www.bankofcanada.ca](http://www.bankofcanada.ca).

(3) Random Lengths Publications Inc. (Western Spruce/Pine/Fir, per thousand board feet).

(4) Average WSPF 2x4 #2 & Btr lumber prices (US $\text{\$}$ ) divided by average exchange rate.

(5) Conifex's EBITDA calculation represents earnings before finance costs, taxes, and depreciation and amortization.

Our quarterly financial results are impacted by a variety of market related factors, including fluctuations in lumber prices and prices of certain commodities related to by-product revenue and manufacturing inputs, changes in the softwood lumber duty deposits rates on shipments to the US, stumpage rates and foreign exchange rates. Other micro-level factors that influence quarterly financial trends include operating rates, shipment volumes, raw material and manufacturing costs and transactions of a non-recurring nature. We rely primarily on third parties for transportation of our products as well as delivery of raw materials, and any significant or prolonged disruption of services provided by third party carriers may adversely impact our operations, cost structure or shipment volumes.

Quarterly trends are also impacted by the seasonal nature of activities such as logging operations and construction and remodelling activity. Our fibre inventories exhibit seasonal swings as we increase log inventories during the fall and winter months to help maintain adequate supply of fibre to our Mackenzie sawmill during the spring months when logging operations are generally largely curtailed due to unstable road conditions. Operating rates are typically lower, and unit manufacturing costs higher, during the fourth quarter of each year due to planned curtailments related to seasonal holidays.

The application of a "time of delivery factor" to the fixed price provided under the EPA generally results in a seasonal effect and considerable variability on quarterly revenues from electricity deliveries, with the lowest revenues generated in the second quarter and the highest in the first and fourth quarters of each year. Quarterly electricity revenues can vary considerably between the strongest and weakest quarters. As a major portion of electricity production costs, as well as interest charges, are fixed in nature, quarterly bioenergy operating results reflect the variability in revenues.

## **OUTLOOK**

We expect a reduction in lumber shipments to follow from the recent announcements of production curtailments from a number of BC lumber producers, sustained robust demand from US housing starts and a recovery of repair and remodelling activities will result in better balanced lumber markets and a gradual recovery of lumber prices through the remainder of the year. At our Mackenzie sawmill, we expect to achieve annualized operating rates of approximately 90% in the third quarter, ramping up to annualized operating rates approaching 100% through the fourth quarter of 2021. Our Mackenzie power plant is forecasted to operate at full capacity and continue to generate a steady and diversified source of cash flow, with seasonally stronger EBITDA contributions expected in the closing quarter of 2021.

As our liquidity and financial position are forecasted to continue to remain strong in the second half of 2021, funding quick payback sawmill upgrades and our NCIB program remain key priorities. We believe that our strengthened liquidity position will allow us to manage any further market volatility that may arise in the coming months.

## **CRITICAL ACCOUNTING ESTIMATES**

We did not make any significant changes to our critical accounting estimates during the quarter ended June 30, 2021. Our critical accounting estimates are described in our MD&A for the year ended December 31, 2020, filed on SEDAR at [www.sedar.com](http://www.sedar.com).

## **RISKS AND UNCERTAINTIES**

A comprehensive discussion of risk factors impacting our business, assets and operations is included in our 2020 annual MD&A dated March 2, 2021, and other filings with the Canadian regulatory authorities available on SEDAR at [www.sedar.com](http://www.sedar.com).

### ***COVID-19 Pandemic***

Given the continuing and dynamic nature of the COVID-19 pandemic, it is challenging to predict its ongoing impact on our business. The extent of any future impacts on our business will depend on new developments related to the virus, including any resurgence of COVID-19 as restrictions are eased or lifted, government and private actions taken to address its impact and new information that may emerge concerning the spread and severity of COVID-19.

## **OUTSTANDING SECURITIES**

As at August 9, 2021, we had 44,696,630 common shares, 2,284,875 long-term incentive plan awards and 3,500,000 warrants outstanding.

**INTERNAL CONTROLS OVER FINANCIAL REPORTING**

During the quarter ended June 30, 2021, there were no changes that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

**ADDITIONAL INFORMATION**

Additional information about our company, including our Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com).