



# International Forest Products Limited

## Second Quarter Report

For the three and six months ended June 30, 2006

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### *Management Discussion and Analysis*

Dated as of July 26, 2006.

This Management Discussion and Analysis (“MD&A”) provides a review of Interfor’s financial performance for the three and six months ended June 30, 2006 relative to 2005, the Company’s financial condition and future prospects. The MD&A should be read in conjunction with the interim Consolidated Financial Statements for the three and six months ended June 30, 2006 and 2005 and Interfor’s Annual Information Form, Consolidated Financial Statements and Annual MD&A for the years ended December 31, 2005 and 2004 filed on SEDAR at [www.sedar.com](http://www.sedar.com). The financial information contained in this MD&A has been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). In the MD&A reference is made to EBITDA and EBITDA excluding Other Income. EBITDA represents earnings before interest, taxes, depletion, amortization and restructuring costs and write-downs of property, plant, equipment and timber. EBITDA excluding Other Income represents EBITDA less other income. The Company discloses EBITDA as it is a measure used by analysts and Interfor’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 financial references in this MD&A are in Canadian dollars.

References in this MD&A to “Interfor” and the “Company” mean International Forest Products Limited, together with its subsidiaries.

### **OPERATING RESULTS**

Interfor recorded net earnings of \$8.0 million or \$0.17 per share in the 2<sup>nd</sup> Quarter of 2006 and net earnings of \$16.8 million or \$0.34 per share for the six months ended June 30, 2006. This compares to net earnings of \$9.0 million or \$0.18 per share in the 2<sup>nd</sup> Quarter of 2005 and net earnings of \$19.9 million or \$0.41 per share for the six months ended June 30, 2005. EBITDA excluding Other Income was \$23.6 million in the 2<sup>nd</sup> Quarter of 2006 and \$43.3 million in the 1<sup>st</sup> Half of 2006 compared to \$23.5 million in the 2<sup>nd</sup> Quarter of 2005 and \$44.6 million in the 1<sup>st</sup> Half of 2005.

Although average lumber and pulp chip prices (as shown in the table “Volume and Price Statistics” below) were lower in the 2<sup>nd</sup> Quarter and 1<sup>st</sup> Half of 2006 compared to 2005, higher lumber production and sales volumes, lower conversion costs in the Company’s sawmills and lower unit logging costs helped to improve the level of operating earnings before considering the impact of restructuring charges and asset write-downs. Operating earnings for the 1<sup>st</sup> Half of 2006 also includes a \$2.1 million recovery of prior years’ stumpage payments.

Lumber shipments totalled 328 and 656 million board feet in the 2<sup>nd</sup> Quarter and 1<sup>st</sup> Half of 2006 respectively compared to 263 and 519 million board feet in the 2<sup>nd</sup> Quarter and 1<sup>st</sup> Half of 2005. The increases in 2006 reflect the addition of the Molalla mill (acquired May 31, 2005) and increased shipments from the Queensboro mill which was rebuilt in the 1<sup>st</sup> Quarter of 2005. Log production in the Company’s B.C. operations was 667,000 and 1,058,000 cubic metres in the 2<sup>nd</sup> Quarter and 1<sup>st</sup> Half of 2006 compared to 765,000 and 1,213,000 cubic metres in the 2<sup>nd</sup> Quarter and 1<sup>st</sup> Half of 2005. Log production in 2006 got off to a slow start due to 1<sup>st</sup> Quarter winter weather related shutdowns on the B.C. Coast.

Sales revenue was \$223.9 million in the 2<sup>nd</sup> Quarter and \$437.5 million in the 1<sup>st</sup> Half of 2006. Sales revenue was \$213.4 million and \$406.3 million in the corresponding periods of 2005. The significantly higher lumber sales volumes in 2006 more than offset declines in average lumber and chip prices (see “Volume and Price Statistics” below)

During the 2<sup>nd</sup> Quarter of 2006 Interfor paid \$5.4 million (\$3.6 million after tax or \$0.07 per share) in deposits for countervailing duty (“CVD”) and antidumping duty (“ADD”) on shipments of 103 million board feet from Canada to the U.S. In the 2<sup>nd</sup> Quarter of 2005 duties totalled \$8.0 million (\$5.1 million after tax or \$0.10 per share) on lumber shipments of 80 million board feet. At the end of the 2<sup>nd</sup> Quarter of 2006, Interfor had paid total deposits of US\$101.6 million (CAD\$113.4 million utilizing June 30, 2006 exchange rates) since the deposit requirement came into effect in May 2002. Total CVD and ADD duties paid for the 1<sup>st</sup> Half of 2006 were \$10.6 million (1<sup>st</sup> Half 2005 - \$14.9 million) on shipments of 210 million board feet (2005 – 141 million board feet). Although volumes shipped to the U.S. are up from 2005 levels the amount of duty is down due to reductions in duty deposit rates and the strengthening of the CAD\$ versus the US\$.

In the 2<sup>nd</sup> Quarter of 2006 Interfor realized a recovery of previously expensed long-term incentive compensation costs of \$1.6 million compared to a recovery of \$1.1 million in the 2<sup>nd</sup> Quarter of 2005. The recoveries were due to decreases in the market value of Interfor’s Class A Subordinate Voting shares.

In the 2<sup>nd</sup> Quarter of 2006 the Company reviewed the valuation of certain B.C. coastal assets which it did not consider to be part of its future core operations. An impairment charge of \$5.9 million was recorded in the quarter to reduce the carrying values of these assets to estimated fair values. The Company continued its programs to improve its competitive cost structure resulting in additional severance charges of \$2.2 million for the quarter and \$3.4 million for the year. These severance charges were reduced by the receipt of \$0.1 million for the quarter, and \$1.7 million for the year, from the B.C. Forestry Revitalization Trust set up by the Government of British Columbia (“the Crown”) as reimbursement for severance costs of workers who were displaced by the reductions in harvesting rights taken under the *Forestry Revitalization Act*. Total

restructuring costs and capital asset write-downs for the 2<sup>nd</sup> Quarter of 2006 were \$8.0 million (2<sup>nd</sup> Quarter 2005 - \$26.5 million). Total restructuring costs and capital asset write-downs for the 1<sup>st</sup> Half of 2006 were \$7.6 million (1<sup>st</sup> Half of 2005 - \$26.5 million).

Equity earnings from Seaboard Shipping Company Limited ("Seaboard") are lower than 2005 levels for both the 2<sup>nd</sup> Quarter and 1<sup>st</sup> Half due to reduced earnings by Seaboard and lower lumber shipments to overseas markets by Interfor.

In June 2006, the Company completed the sale of several properties in Squamish, B.C. for proceeds of \$10.5 million. The gain of \$8.5 million is included in Other Income for the 2<sup>nd</sup> Quarter of 2006. In addition, Interfor disposed of other surplus property, plant and equipment in the 2<sup>nd</sup> Quarter of 2006. The following table shows the components of other income for 2006 and 2005:

	3 Months June 30, 2006		3 Months June 30, 2005		6 Months June 30, 2006		6 Months June 30, 2005	
	(millions of dollars)							
Gain on disposal of surplus property, plant and equipment	\$	10.1	\$	1.9	\$	12.6	\$	2.5
Gain on settlement of timber takeback		-		-		-		6.4
Equity income participation in gain on disposal of Western Stevedoring		-		19.5		-		19.5
Other		-		-		0.5		-
	\$	10.1	\$	21.4	\$	13.1	\$	28.4

### SELECTED QUARTERLY FINANCIAL INFORMATION

	2006 Qtr 2	2006 Qtr 1	2005 Qtr 4	2005 Qtr 3	2005 Qtr 2	2005 Qtr 1	2004 Qtr 4	2004 Qtr 3
	(millions of dollars except share and per share amounts)							
Sales - Lumber	173.5	177.7	171.3	166.2	161.8	162.1	165.6	181.0
- Logs	21.4	14.6	23.3	26.7	30.4	17.3	29.2	37.6
- Wood chips and other by-products	9.3	9.1	8.6	9.0	8.3	8.2	9.4	11.1
- Other	19.7	12.2	11.5	12.3	12.9	5.3	8.5	9.3
Total Sales	223.9	213.6	214.7	214.2	213.4	192.9	212.7	239.0
Operating earnings (loss) before restructuring costs and asset write-downs	8.3	8.5	(0.6)	(2.8)	6.6	7.1	-	12.5
Operating earnings (loss)	0.3	8.9	(14.7)	(4.0)	(19.9)	7.1	(5.3)	(7.7)
Net earnings (loss)	8.0	8.7	(4.9)	4.7	9.0	10.9	15.2	(3.1)
Net earnings (loss) per share - basic	0.17	0.18	(0.10)	0.10	0.18	0.22	0.31	(0.06)
- diluted	0.16	0.18	(0.10)	0.10	0.18	0.22	0.31	(0.06)
EBITDA <sup>3</sup>	33.7	22.7	19.7	23.6	44.9	28.1	33.7	31.2
EBITDA excluding Other Income	23.6	19.7	16.3	13.8	23.5	21.2	15.0	31.2
Cash flow from operations <sup>1</sup> per share	0.43	0.38	0.03	0.17	0.43	0.36	0.19	0.44
Shares outstanding - end of period (millions) <sup>2</sup>	48.4	48.7	48.7	48.7	48.7	48.7	48.6	48.4
- weighted average (millions)	48.6	48.7	48.7	48.7	48.7	48.7	48.5	48.4

1 Cash generated from operations before considering changes in operating working capital.

2 As at July 26, 2006 the number of shares outstanding by class are: Class A Subordinate Voting shares - 47,396,496, Class B Common shares - 1,015,779, Total - 48,412,275.

3 EBITDA represents earnings before interest, taxes, depletion, amortization and restructuring costs and write-downs of property, plant, equipment and timber. The Company discloses EBITDA as it is a measure used by analysts and Interfor'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. EBITDA and EBITDA excluding Other Income can be calculated from the statement of operations as follows:

Net earnings (loss)	8.0	8.7	(4.9)	4.7	9.0	10.9	15.2	(3.1)
Add: Income taxes (recovery)	2.1	3.0	(6.3)	0.7	(6.5)	4.9	(1.4)	(2.5)
Interest expense	1.0	1.0	1.3	1.3	1.0	1.0	1.3	1.0
Depletion and amortization	14.6	10.4	15.5	15.8	14.9	11.3	13.3	15.7
Restructuring costs, asset write-downs and other	8.0	(0.4)	14.1	1.1	26.5	-	5.3	20.1
EBITDA	33.7	22.7	19.7	23.6	44.9	28.1	33.7	31.2
Deduct: Other income	(10.1)	(3.0)	(3.4)	(9.8)	(21.4)	(6.9)	(18.7)	-
EBITDA excluding Other Income	23.6	19.7	16.3	13.8	23.5	21.2	15.0	31.2

### Volume and Price Statistics

	2006 Qtr 2	2006 Qtr 1	2005 Qtr 4	2005 Qtr 3	2005 Qtr 2	2005 Qtr 1	2004 Qtr 4	2004 Qtr 3
Lumber sales (million fbm)	328	328	333	308	263	256	272	238
Lumber production <sup>1</sup> (million fbm)	326	325	316	308	266	253	246	247
Log Sales <sup>2</sup> (thousand cubic metres)	224	178	323	363	379	184	350	438
Log production (B.C. operations) (thousand cubic metres)	667	391	634	712	765	447	573	891
Average price - lumber <sup>3</sup> (\$/thousand fbm)	\$530	\$540	\$514	\$539	\$615	\$633	\$609	\$759
Average price - logs <sup>2</sup> (\$/cubic metre)	\$95	\$81	\$71	\$73	\$80	\$84	\$79	\$86
Average price - pulp chips (\$/thousand fbm)	\$26	\$25	\$24	\$25	\$27	\$29	\$33	\$40

1 Excludes lumber produced on a custom cutting basis for customers who have previously purchased the logs

2 B.C. coastal operations

3 Gross sales before countervailing and antidumping duties

Quarterly trends normally reflect seasonality of the Company's operations. Logging operations are seasonal due to a number of factors including weather, ground conditions and fire season woods closures. Generally, the Company's logging divisions experience higher production levels in the latter half of the first quarter, throughout the second and third quarters and in the first half of the fourth quarter. Sawmill operations are less seasonal than logging operations but do depend on the availability of logs from the logging operations. In addition, the market demand for lumber and related products is generally lower in the first quarter due to reduced construction activity which increases during the spring, summer and fall. The significant increase in earnings in the fourth quarter of 2004 was largely due to an increase in Other Income, consisting of gains on surplus property sales and a break fee earned on the attempted acquisition of Riverside Forest Products Limited. The declines in operating earnings and net earnings in the last two quarters of 2005 was largely a result of declines in product selling prices and the continued strengthening of the Canadian dollar against the U.S. dollar.

### **UUCASH FLOW AND FINANCIAL POSITION**

During the 2<sup>nd</sup> Quarter of 2006 Interfor generated \$21.1 million (2<sup>nd</sup> Quarter of 2005 - \$21.0 million) in cash from operations before changes in working capital, and \$20.7 million (2<sup>nd</sup> Quarter of 2005 - \$13.5 million) after changes in working capital were considered. Cash used in working capital in the 2<sup>nd</sup> Quarter of 2006 included \$4.0 million related to increased accounts receivable balances. This increase was due to a decrease in the Company's accounts receivable securitization program of \$5.0 million. At June 30, 2006, the Company received cash proceeds of \$20.0 million (December 31, 2005 and June 30, 2005 - \$25.0 million) from the sale of receivables under this program. Effective July 17, 2006, the Company temporarily reduced its sales of receivables to nil.

Cash flow from operations including working capital changes for the 1<sup>st</sup> Half of 2006 was \$36.1 million (1<sup>st</sup> Half of 2005 - \$31.8 million). Cash from operations before changes in operating working capital was similar to the 1<sup>st</sup> Half of 2005.

Capital spending in the 2<sup>nd</sup> Quarter of 2006 amounted to \$26.2 million (2<sup>nd</sup> Quarter of 2005 - \$19.7 million) including \$7.4 million in roads and timber, \$3.4 million in maintenance capital, \$14.6 million in high return discretionary projects and \$0.8 million in land development costs. Capital spending for the 1<sup>st</sup> Half of 2006 totalled \$42.1 million (1<sup>st</sup> Half of 2005 - \$43.6 million).

Proceeds from disposals of property, plant and equipment in the 2<sup>nd</sup> Quarter of 2006 totalled \$16.0 million and included \$10.5 million from the sale of surplus properties in Squamish, B.C. and \$5.5 million from the sale of other surplus properties, the Saltair Timber Products Ltd. remanufacturing plant in Chemainus, B.C. and other surplus logging and manufacturing equipment. In the 2<sup>nd</sup> Quarter of 2005, Interfor received \$2.3 million of proceeds from the sale of surplus logging and manufacturing equipment.

Proceeds from disposals of property, plant and equipment in the 1<sup>st</sup> Half of 2006 totalled \$21.1 million (1<sup>st</sup> Half of 2005 - \$24.3 million). The 1<sup>st</sup> Half of 2005 included \$20.8 million of proceeds from settlement of the Province of B.C. timber takeback.

In the 2<sup>nd</sup> Quarter of 2006, the Company renewed its existing Canadian operating line of credit. The terms and conditions of the line remain the same, except both the maximum operating line of credit and the interest rate premiums were reduced. The new maximum as at June 30, 2006 was \$60.0 million (June 30, 2005 - \$75.0 million). The line matures on April 26, 2007.

The maximum borrowing available under the Company's Canadian revolving term line ("Revolving Line") at June 30, 2006 was \$90.0 million (June 30, 2005 - \$90.0 million). As at June 30, 2006, the Revolving Line was undrawn (June 30, 2005 - US\$25.0 million revalued to CAD\$30.6 million). The Revolving Line matures on April 27, 2007. Effective July 12, 2006, the Company reduced the maximum available credit under the Canadian revolving term line to \$40.0 million. As at June 30, 2006, the \$US non-revolving term line (the "Non-Revolving Line") remains fully drawn at US\$35.0 million (June 30, 2005 - US\$35.0 million) and was revalued at the month-end exchange rate to CAD\$39.1 million (June 30, 2005 - CAD\$42.9 million). The Non-Revolving Line matures on September 1, 2009.

Interfor's net debt was \$13.7 million at June 30, 2006 (December 31, 2005 - \$29.7 million and June 30, 2005 - \$87.7 million), representing a ratio of net debt to invested capital of 3.3% compared to 18.3% at the end of the 2<sup>nd</sup> Quarter of 2005, and 7.1% at December 31, 2005. The net debt amounts and ratios for 2005 exclude short term advances from the Seaboard Limited Partnership of \$27.8 million at June 30, 2005 and \$54.4 million at December 31, 2005. These advances were repaid January 3, 2006 by way of setoff against an income distribution from the Seaboard Limited Partnership. At June 30, 2006, after giving effect to the reduction in the Revolving Line referred to above, the Company's available credit under its various operating lines and term lines totalled approximately \$111.0 million. In addition, at June 30, 2006 the Company had cash balances of \$25.4 million.

### **UNORMAL COURSE ISSUER BID**

On November 9, 2005, the Company commenced a normal course issuer bid to acquire up to 2,384,000 Class A Subordinate Voting shares ("Class A Shares") (representing approximately 5% of the outstanding Class A Shares) through the facilities of the Toronto Stock Exchange. Purchases are made at market prices with a maximum of 2% of the outstanding Class A Shares being purchased in any 30-day period. During the 2<sup>nd</sup> Quarter of 2006 386,600 Class A Shares were purchased at an average price of \$6.95 per share. No Class A Shares were purchased under the normal course issuer bid during the 1<sup>st</sup> Quarter of 2006. The normal course issuer bid will terminate no later than November 8, 2006. A copy of the Notice of Intention to Make a Normal Course Issuer Bid is available from the Company without charge.

### **ASSETS HELD FOR SALE**

As at June 30, 2006, the company has classified the assets and liabilities of the following operations as assets held for sale:

1. MacKenzie sawmill  
On June 23, 2006 Interfor announced an agreement for the sale of its MacKenzie sawmill located in Surrey, B.C. The sale is subject to the finalization of financial arrangements by the purchaser and is scheduled to close in the 3<sup>rd</sup> Quarter of 2006.
2. Helicopter logging operations  
In the 1<sup>st</sup> Quarter of 2006 the Company announced an agreement to sell its helicopter logging operations for \$4.0 million plus an amount for working capital and additional amounts of up to \$1.5 million dependent upon future helicopter logging services. The transaction has not yet received Canadian Transportation Agency approval and is now expected to close in the 3<sup>rd</sup> Quarter of 2006.

## **B.C. INTERIOR STUMPAGE CHANGE**

On April 6, 2006 the Crown announced a new market-based timber pricing system for the B.C. Interior. The new market-based timber pricing system will use B.C. Timber Sales auction data to set stumpage prices. It replaces the previous system which used Statistics Canada lumber and chip price indices. The Crown anticipates the new pricing system will be more responsive to market changes and will better reflect global markets and local harvesting costs. The new pricing system was originally scheduled to be effective September 1, 2006 but the Crown accelerated the implementation and it became effective July 1, 2006.

## **CANADA – U.S. SOFTWOOD LUMBER DISPUTE**

On November 23, 2005 Interfor was selected by the U.S. Department of Commerce (“USDOC”) as a mandatory respondent in the third administrative review of the antidumping duty order on softwood lumber products from Canada (“ADD AR3”). As a mandatory respondent, the U.S. Department of Commerce (“USDOC”) will calculate a company-specific ADD for the review period May 1, 2004 to April 30, 2005. In June the USDOC released a Notice of Preliminary Results of the Review which indicated Interfor’s ADD rate would be 6.46%. The Company will be disputing the USDOC preliminary findings with respect to USDOC clerical errors and calculation methodology. The ADD AR3 is expected to be completed in late 2006 at which time Interfor will be assigned a final Company-specific ADD rate for the review period. This rate will also remain effective as a deposit rate for the Company until the release of the final results of the Fourth Administrative Review in late 2007.

Effective December 12, 2005, the USDOC implemented new deposit rates based on the USDOC’s final rate determinations for the Second Administrative Review period (April 1, 2003 to March 31, 2004 for the CVD case; and May 1, 2003 to April 30, 2004 for the ADD case). The USDOC reduced the CVD deposit rate to 8.70% from 16.37% and reduced the all others ADD deposit rate to 2.11% from 3.78%. The ADD rate was subsequently amended by the USDOC effective January 23, 2006, reducing the rate to 2.10%. At the date of this report the Company’s combined CVD and ADD deposit rate is 10.80%.

Interfor and other Canadian forest product companies, the Federal Government and Canadian provincial governments (together, “Canadian Interests”) categorically deny U.S. allegations which result in the imposition of the CVD and ADD. While exploring the possibility of a negotiated settlement to the dispute, Canadian Interests continue to pursue appeals of the final CVD and ADD determinations with the appropriate courts, NAFTA panels and the World Trade Organization. As such, the actual amount of duties for softwood lumber products shipped will depend upon the outcome of these various appeals or upon a negotiated settlement.

On April 27, 2006 the federal governments of Canada and the United States reached a framework agreement to resolve the softwood lumber dispute. On July 1, 2006 Canada and the United States agreed on the legal text of the agreement. The proposed agreement provides for the return of approximately 80% of duties paid, plus interest. The agreement has a term of seven years and provides for an extension of two years and for early termination by either government after two years. Canadian softwood lumber exporters will pay an export charge when the price of lumber is at or below US\$355 per thousand board feet, as determined by the Random Lengths Framing Lumber Composite Price. The Province of B.C. will have the right to choose between an export charge only or a lower export charge with a quota. This choice will be made separately for the B.C. Coast and B.C. Interior regions. A significant number of Canadian forest product companies and provincial governments have indicated that unless certain changes are made to the agreement they may not support the agreement and may refuse to withdraw their legal challenges. As of the date of this report it is not possible to determine whether a final settlement will be reached and whether the terms of the potential agreement will be varied.

## **OUTLOOK**

The cumulative effect of 2005 and 2006 interest rate increases and lower housing starts in the U.S. contributed to a significant decline in structural lumber prices in the North American market in the 2<sup>nd</sup> Quarter. Interfor expects that structural lumber prices will remain under pressure for the remainder of 2006 with little likelihood of significant increases. Cedar lumber prices are expected to remain at or near current levels but will be sensitive to supply. Lumber prices in Japan have risen in the 1<sup>st</sup> Half of 2006 and Interfor expects prices to remain firm as housing starts have increased and the relationship of the Japanese Yen to the US\$ has remained fairly flat through the 1<sup>st</sup> Half.

As discussed above under “CANADA – U.S. SOFTWOOD LUMBER DISPUTE” the likelihood of the Company receiving a duty refund cannot be determined at this time.

Interfor’s initiative to monetize non-core and non-performing assets and to streamline its organization structure will continue. The Company expects to operate its sawmills on a normal schedule in the 3<sup>rd</sup> Quarter.

## **FORWARD LOOKING STATEMENTS**

This report contains statements that are forward-looking in nature. Such statements involve known and unknown risks and uncertainties that may cause the actual results of the Company to be materially different from those expressed or implied by those forward-looking statements. Such risks and uncertainties include, among others: general economic and business conditions, product selling prices, raw material and operating costs, changes in foreign-currency exchange rates and other factors referenced herein and in the Company’s annual statutory report.

## **ADDITIONAL INFORMATION**

Additional information relating to the Company and its operations, including Interfor’s Annual Statutory Information for 2005, can be found on its website at [www.interfor.com](http://www.interfor.com) and on SEDAR at [www.sedar.com](http://www.sedar.com). Interfor’s trading symbol on the Toronto Stock Exchange (“TSX”) is IFP.A.



William L. Sauder  
Chairman



Duncan K. Davies  
President and Chief Executive Officer



## CONSOLIDATED STATEMENTS OF OPERATIONS

For the three and six months ended June 30, 2006 and 2005 (unaudited)

(thousands of Canadian dollars except earnings per share)

	3 Months June 30, 2006	3 Months June 30, 2005	6 Months June 30, 2006	6 Months June 30, 2005
<b>Sales</b>	\$ 223,907	\$ 213,408	\$ 437,510	\$ 406,334
<b>Costs and expenses:</b>				
Production	192,367	179,857	376,139	340,373
Selling and administration	4,893	5,130	9,895	10,590
Long term incentive compensation	(1,596)	(1,122)	(841)	606
U.S. countervailing and antidumping duty deposits (note 11)	5,397	8,013	10,574	14,899
Amortization of plant and equipment	7,418	6,372	15,049	12,518
Depletion and amortization of timber, roads and other	7,153	8,567	9,941	13,673
	215,632	206,817	420,757	392,659
<b>Operating earnings before restructuring costs</b>	8,275	6,591	16,753	13,675
Restructuring costs and write-downs of property, plant, equipment and timber (note 7)	7,990	26,461	7,577	26,461
<b>Operating earnings (loss)</b>	285	(19,870)	9,176	(12,786)
Interest expense on long-term debt	(800)	(820)	(1,562)	(1,584)
Other interest expense	(230)	(216)	(472)	(490)
Other income (note 6)	10,125	21,417	13,092	28,359
Equity in earnings of investee companies	715	1,948	1,559	4,780
	9,810	22,329	12,617	31,065
<b>Earnings before income taxes</b>	10,095	2,459	21,793	18,279
<b>Income tax expense (recovery):</b>				
Current	(686)	249	(53)	2,334
Future	2,747	(6,750)	5,084	(3,936)
	2,061	(6,501)	5,031	(1,602)
<b>Net earnings</b>	\$ 8,034	\$ 8,960	\$ 16,762	\$ 19,881
<b>Net earnings per share (note 9)</b>				
Basic	\$ 0.17	\$ 0.18	\$ 0.34	\$ 0.41
Diluted	\$ 0.16	\$ 0.18	\$ 0.34	\$ 0.40

See accompanying notes to consolidated financial statements

## CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

For the six months ended June 30, 2006 and 2005 (unaudited)

(thousands of Canadian dollars)

	6 Months June 30, 2006	6 Months June 30, 2005
<b>Retained earnings, beginning of year</b>	\$ 85,943	\$ 66,218
<b>Net earnings</b>	16,762	19,881
<b>Retained earnings, end of period</b>	\$ 102,705	\$ 86,099

See accompanying notes to consolidated financial statements



**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**For the three and six months ended June 30, 2006 and 2005 (unaudited)**

(thousands of Canadian dollars)	3 Months June 30, 2006	3 Months June 30, 2005	6 Months June 30, 2006	6 Months June 30, 2005
<b>Cash provided by (used in):</b>				
<b>Operating activities:</b>				
<b>Net earnings</b>	\$ 8,034	\$ 8,960	\$ 16,762	\$ 19,881
<b>Items not involving cash:</b>				
Amortization of plant and equipment	7,418	6,372	15,049	12,518
Depletion and amortization of timber, roads and other	7,153	8,567	9,941	13,673
Future income taxes	2,747	(6,750)	5,084	(3,936)
Reforestation liability	857	6	2,076	979
Other long-term liabilities	(166)	(804)	(814)	(1,963)
Equity in earnings of investee companies	(715)	(1,948)	(1,559)	(4,780)
Write-downs of property, plant, equipment and timber	5,868	28,007	5,868	30,277
Other (note 6)	(10,125)	(21,413)	(12,650)	(28,342)
	<b>21,071</b>	<b>20,997</b>	<b>39,757</b>	<b>38,307</b>
<b>Cash generated from (used in) operating working capital:</b>				
Accounts receivable	(4,036)	(11,809)	(7,710)	(9,306)
Inventories	1,076	7,066	7,995	6,000
Prepaid expenses	(712)	202	(2,397)	2,102
Accounts payable and accrued liabilities	4,902	(199)	(284)	(4,507)
Income taxes	(1,567)	(2,722)	(1,259)	(777)
	<b>20,734</b>	<b>13,535</b>	<b>36,102</b>	<b>31,819</b>
<b>Investing activities:</b>				
Additions to property, plant and equipment	(18,752)	(12,578)	(31,683)	(31,488)
Additions to logging roads and timber	(7,410)	(5,987)	(10,405)	(10,988)
Additions to deferred start-up costs	-	(1,115)	-	(1,115)
Proceeds on disposal of property, plant, equipment, timber and roads	16,045	2,298	21,060	24,258
Acquisitions	-	(79,905)	-	(79,905)
Cash received on acquisition of subsidiary	-	2,650	-	2,650
Investments and other assets	(45)	(107)	1,776	5,698
	<b>(10,162)</b>	<b>(94,744)</b>	<b>(19,252)</b>	<b>(90,890)</b>
<b>Financing activities:</b>				
Issuance of share capital, net of expenses	385	37	525	190
Repurchase of share capital	(2,695)	-	(2,695)	-
Increase (decrease) in bank indebtedness	(10,072)	14,150	(8,053)	14,150
Funds from promissory note payable to investee company	-	27,757	-	27,757
Additions to long-term debt	-	31,405	-	31,405
Repayments of long-term debt	-	(12,396)	-	(32,910)
	<b>(12,382)</b>	<b>60,953</b>	<b>(10,223)</b>	<b>40,592</b>
<b>Foreign exchange (gain) loss on cash and cash equivalents held in a foreign currency:</b>	<b>(440)</b>	<b>146</b>	<b>(313)</b>	<b>220</b>
<b>Increase (decrease) in cash</b>	<b>(2,250)</b>	<b>(20,110)</b>	<b>6,314</b>	<b>(18,259)</b>
<b>Cash on deposit, beginning of period</b>	<b>27,625</b>	<b>20,110</b>	<b>19,061</b>	<b>18,259</b>
<b>Cash on deposit, end of period</b>	<b>\$ 25,375</b>	<b>\$ -</b>	<b>\$ 25,375</b>	<b>\$ -</b>
<b>Supplementary disclosures (see also note 4)</b>				
Cash interest paid	\$ 1,030	\$ 1,036	\$ 2,034	\$ 2,074
Cash income taxes paid	881	3,032	1,206	3,176

See accompanying notes to consolidated financial statements



## CONSOLIDATED BALANCE SHEETS

June 30, 2006 and 2005 (unaudited) and December 31, 2005 (audited)

(thousands of Canadian dollars)

	June 30, 2006	December 31, 2005	June 30, 2005
<b>Assets</b>			
<b>Current assets:</b>			
Cash	\$ 25,375	\$ 19,061	\$ -
Accounts receivable (note 13(c))	45,621	37,911	55,808
Income taxes recoverable	1,884	625	263
Inventories	90,773	102,960	113,107
Prepaid expenses	7,957	6,439	8,254
Future income taxes	4,493	6,659	5,060
Current assets held for sale (note 3)	5,071	-	-
	181,174	173,655	182,492
<b>Investments and other assets</b>			
Investments and advances (note 4)	7,389	62,370	55,990
Deferred financing fee, net of accumulated amortization	299	377	526
	7,688	62,747	56,516
<b>Property, plant and equipment, net of accumulated amortization</b>	283,770	289,227	299,548
<b>Timber and logging roads, net of accumulated depletion and amortization</b>	52,704	52,375	63,476
<b>Goodwill and other intangible assets</b>	13,135	15,694	15,733
<b>Future income taxes</b>	1,843	3,980	-
<b>Long-lived assets held for sale (note 3)</b>	4,899	-	-
	\$ 545,213	\$ 597,678	\$ 617,765
<b>Liabilities and Shareholders' Equity</b>			
<b>Current liabilities:</b>			
Bank indebtedness (note 5(a))	\$ -	\$ 8,053	\$ 14,150
Accounts payable and accrued liabilities	82,401	82,685	82,408
Promissory note payable to investee company (note 4)	-	54,354	27,757
Future income taxes payable	-	351	-
	82,401	145,443	124,315
<b>Reforestation liability, net of current portion</b>	17,318	15,242	17,961
<b>Long-term debt (note 5(b))</b>	39,067	40,705	73,524
<b>Other long-term liabilities</b>	5,853	6,667	7,470
<b>Future income taxes</b>	3,569	3,100	2,592
<b>Shareholders' equity:</b>			
Share capital (note 8)			
Class A subordinate voting shares	292,819	294,683	294,771
Class B common shares	4,080	4,080	4,080
Contributed surplus	7,880	8,186	8,201
Cumulative translation adjustment	(10,479)	(6,371)	(1,248)
Retained earnings	102,705	85,943	86,099
	397,005	386,521	391,903
	\$ 545,213	\$ 597,678	\$ 617,765

Contingencies (note 11)

Subsequent events (notes 5(b) and 13(c))

See accompanying notes to consolidated financial statements

On behalf of the Board:

W. L. Sauder  
Director

H. C. Kalke  
Director

## INTERNATIONAL FOREST PRODUCTS LIMITED

Notes to Unaudited Interim Consolidated Financial Statements  
(Tabular amounts expressed in thousands except per share amounts)  
Three and six months ended June 30, 2006 and 2005 (unaudited)

### 1. Significant accounting policies:

These unaudited interim consolidated financial statements include the accounts of International Forest Products Limited and its subsidiaries (collectively referred to as "Interfor" or the "Company"). These interim consolidated financial statements do not include all disclosures required by Canadian generally accepted accounting principles for annual financial statements, and accordingly, these interim consolidated financial statements should be read in conjunction with Interfor's most recent annual consolidated financial statements. These interim consolidated financial statements follow the same accounting policies and methods of application used in the Company's audited annual consolidated financial statements as at and for the year ended December 31, 2005.

### 2. Seasonality of operating results:

The Company operates in the solid wood business which includes logging and manufacturing operations. Logging activities vary throughout the year due to a number of factors including weather, ground and fire season conditions. Generally, the Company operates its logging divisions in the latter half of the first quarter, throughout the second and third quarters and in the first half of the fourth quarter. Manufacturing operations are less seasonal than logging operations but do depend on the availability of logs from the logging operations and from third party suppliers. In addition, the market demand for lumber and related products is generally lower in the first quarter due to reduced construction activity which increases during the spring, summer and fall.

### 3. Assets held for sale:

On February 10, 2006, the Company signed an agreement to sell its helicopter logging operations, conducted by its wholly-owned subsidiary, Helifor Industries Limited. The transaction is subject to Canadian Transportation Agency approval and is expected to close prior to the year-end.

On June 23, 2006, the Company reached an agreement for the sale of its MacKenzie sawmill assets. The sale is subject to the purchaser concluding its financial arrangements and is scheduled to close in the third quarter of 2006.

As at June 30, 2006, the company has classified the assets of these operations as assets held for sale.

### 4. Payable to investee company:

On April 21, 2005, the Seaboard Limited Partnership ("the Seaboard Partnership"), made an advance to its partners, with the Company's share of the advance being \$27,757,000. The Company signed an unsecured promissory note which was payable on demand on or before January 31, 2006 and was non-interest bearing until January 31, 2006 and interest bearing at the rate of 5% per annum thereafter.

On December 29, 2005, the Seaboard Partnership provided a second advance to its partners, with the Company's share of this advance being \$26,597,000. The advance was payable on demand and was non-interest bearing.

On January 3, 2006, the Seaboard Partnership declared an income distribution to its partners, of which the Company's share of \$54,354,000 was received by way of setoff against the advance and the promissory note payable to the Seaboard Partnership. In accordance with equity accounting, the income distribution was recorded as a reduction of the investment in Seaboard.

### 5. Bank indebtedness and long-term debt:

#### (a) Bank indebtedness:

	Canadian Operating Facility	Mapri Developments	U.S. Operating Facility	Total
June 30, 2006				
Available line of credit	\$ 60,000	\$ 4,000	\$ 16,743	\$ 80,743
Maximum borrowing available	54,868	4,000	16,743	75,611
Unused portion of line	50,392	4,000	16,609	71,001
Outstanding letters of credit included in line utilization	4,476	-	134	4,610
June 30, 2005				
Available line of credit	\$ 75,000	\$ 4,000	\$ 18,381	\$ 97,381
Maximum borrowing available	70,066	4,000	18,381	92,447
Unused portion of line	51,600	4,000	14,876	70,476
Outstanding letters of credit included in line utilization	4,283	-	441	4,724

In the second quarter of 2006, the Company renewed its existing Canadian operating line of credit. The terms and conditions of the line remain unchanged, except for a reduction in the interest rate premiums, and a reduction in the maximum operating credit available to \$60,000,000 (June 30, 2005 - \$75,000,000). The line is subject to a borrowing base calculation dependent upon certain accounts receivable and inventories. The loan bears interest at bank prime plus a premium depending upon a financial ratio or, at the Company's option, at rates for Bankers' Acceptances. The line of credit is secured and is subject to certain financial covenants including a minimum working capital requirement and a maximum ratio of total debt to total capitalization.

## INTERNATIONAL FOREST PRODUCTS LIMITED

Notes to Unaudited Interim Consolidated Financial Statements  
(Tabular amounts expressed in thousands except per share amounts)  
Three and six months ended June 30, 2006 and 2005 (unaudited)

### 5. Bank indebtedness and long-term debt (continued):

#### (a) Bank indebtedness (continued):

In the first quarter of 2006, the Company renewed its existing U.S. operating line of credit. The terms and conditions of the line remain unchanged, with a maximum operating line of credit totalling US\$15,000,000. The line is subject to a borrowing base calculation dependent upon certain accounts receivable and inventories of the Company's subsidiary, Interfor Pacific Inc. The loan bears interest at U.S. bank prime or, at the Company's option, at LIBOR plus 1¼%. The line of credit is secured by the accounts receivables and inventories of Interfor Pacific Inc. and is subject to certain financial covenants including a maximum ratio of total debt to total capitalization. The line matures on March 1, 2007.

On acquisition of Mapri Developments Ltd. ("Mapri") on May 31, 2005, the Company renewed Mapri's existing revolving line of credit of \$4,000,000. This demand line bears interest at bank prime plus ¼%, and, after renegotiation in the first quarter of 2006, is secured by a general charge over all assets of B.W. Creative Wood Industries Ltd., a wholly-owned subsidiary of Mapri. The line is subject to a borrowing base calculation dependent upon certain accounts receivable and inventories and matures on August 1, 2006.

#### (b) Long-term debt:

The maximum borrowing available under the Company's Canadian revolving term line ("Revolving Line") is \$90,000,000 (June 30, 2005 - \$90,000,000). As at June 30, 2006, the Revolving Line was undrawn (June 30, 2005 - US\$25,000,000 revalued to CAD\$30,635,000). The Revolving Line bears interest at rates based on bank prime plus a premium, depending upon a financial ratio or, at the Company's option, at rates for Bankers' Acceptances or LIBOR based loans and matures on April 27, 2007. Effective July 12, 2006, the Company reduced the maximum borrowing available under this facility to \$40,000,000.

As at June 30, 2006, the \$US non-revolving term line (the "Non-Revolving Line") remains fully drawn at US\$35,000,000 (June 30, 2005 - US\$35,000,000) and was revalued at the month-end exchange rate to CAD\$39,067,000 (June 30, 2005 - CAD\$42,889,000). The Non-Revolving Line bears interest at rates based on bank prime plus a premium depending upon a financial ratio or, at the Company's option, at rates for LIBOR based loans and matures on September 1, 2009.

Both lines are secured and are subject to certain financial covenants including a minimum working capital requirement and a maximum ratio of total debt to total capitalization.

Minimum principal amounts due on long-term debt within the next five years are as follows:

2006	\$	-
2007		-
2008		-
2009		39,067
2010		-
	\$	39,067

### 6. Other income:

	3 months June 30, 2006	3 months June 30, 2005	6 months June 30, 2006	6 months June 30, 2005
Gain on disposal of Marysville sawmill	\$ -	\$ -	\$ 874	\$ -
Gain on disposal of surplus Squamish properties	8,534	-	8,534	-
Gain on disposal of other surplus property, plant and equipment	1,574	1,916	3,225	2,485
Gain on settlement of timber takeback	-	-	-	6,373
Equity income participation in gain on disposal of Western Stevedoring	-	19,501	-	19,501
Other income	17	-	459	-
	\$ 10,125	\$ 21,417	\$ 13,092	\$ 28,359

During the second quarter, 2006, the Company completed the sale of surplus properties in Squamish, B.C. for sale proceeds of \$10,533,000 and a gain of \$8,534,000. In addition, all property, plant and equipment of Saltair Timber Products Limited and surplus equipment of Field Sawmill division on Vancouver Island, B.C. as well as surplus logging and other assets were sold in the quarter for proceeds of \$4,730,000 and a gain of \$1,574,000.

In the first quarter, the Company completed the sale of its sawmill located in Marysville, Washington. The Company recorded sale proceeds of \$2,542,000 and a gain of \$874,000.

## INTERNATIONAL FOREST PRODUCTS LIMITED

### Notes to Unaudited Interim Consolidated Financial Statements

(Tabular amounts expressed in thousands except per share amounts)

Three and six months ended June 30, 2006 and 2005 (unaudited)

#### 7. Restructuring costs and write-downs of property, plant, equipment and timber:

	3 Months June 30, 2006	3 Months June 30, 2005	6 months June 30, 2006	6 months June 30, 2005
Property, plant, equipment and timber write-downs	\$ 5,868	\$ 28,007	\$ 5,868	\$ 30,277
Severance and other restructuring costs (recoveries)	2,122	(1,546)	1,709	(1,546)
Other (recoveries)	-	-	-	(2,270)
	\$ 7,990	\$ 26,461	\$ 7,577	\$ 26,461

In the second quarter, 2006, the Company reviewed the valuation of certain B.C. coastal assets which it did not consider to be part of its future core operations. An impairment charge of \$5,868,000 was recorded in the quarter to reduce the carrying values of these assets to estimated fair values. The Company continued its programs to improve its competitive cost structure resulting in additional severance charges of \$2,193,000 for the quarter (\$3,396,000 for the six months).

During the first and second quarters, 2006, the Company received recoveries totalling \$1,687,000 from the B.C. Forestry Revitalization Trust set up by the Government of British Columbia, as reimbursement for severance costs of workers who were displaced by the reductions in harvesting rights taken under the *Forestry Revitalization Act*. As the associated costs had been expensed in the current and prior years as restructuring costs, the recovery served to offset additional severance costs for these workers recorded in the current year to date. The Company continues to pursue mitigation of certain restructuring costs which it feels it is entitled to under the terms of the Trust, but the amount of any additional mitigation is not yet determinable and will be recorded when the amounts can be estimated.

#### 8. Share capital:

On November 9, 2005, the Company commenced a normal course issuer bid to acquire up to 2,384,000 Class A Subordinate Voting shares ("Class A Shares") (representing approximately 5% of the outstanding Class A Shares) through the facilities of the Toronto Stock Exchange. Purchases are made at market prices with a maximum of two percent of the outstanding Class A Shares being purchased in any 30-day period. During the second quarter of 2006 the Company acquired 386,600 Class A shares at a total cost of \$2,695,000 and the shares were cancelled as purchased. The excess of the cost of the shares over the assigned value totaled \$306,000 and has been charged to contributed surplus. No Class A Shares were purchased under the normal course issuer bid during the 1st Quarter of 2006. The normal course issuer bid will terminate no later than November 8, 2006.

#### 9. Net earnings per share:

	3 months June 30, 2006			3 months June 30, 2005		
	Net earnings	Shares	Per share	Net earnings	Shares	Per share
Basic earnings per share	\$ 8,034	48,639	\$ 0.17	\$ 8,960	48,678	\$ 0.18
Share options	-	662	-	-	629	-
Diluted earnings per share	\$ 8,034	49,301	\$ 0.16	\$ 8,960	49,307	\$ 0.18

  

	6 months June 30, 2006			6 months June 30, 2005		
	Net earnings	Shares	Per share	Net earnings	Shares	Per share
Basic earnings per share	\$ 16,762	48,660	\$ 0.34	\$ 19,881	48,667	\$ 0.41
Share options	-	644	-	-	653	-
Diluted earnings per share	\$ 16,762	49,304	\$ 0.34	\$ 19,881	49,320	\$ 0.40

## INTERNATIONAL FOREST PRODUCTS LIMITED

Notes to Unaudited Interim Consolidated Financial Statements  
(Tabular amounts expressed in thousands except per share amounts)  
Three and six months ended June 30, 2006 and 2005 (unaudited)

### 10. Segmented information:

The Company manages its business as a single operating segment, solid wood. The Company purchases and harvests logs which are then manufactured into lumber products at the Company's sawmills, or sold. Substantially all of the Company's operations are located in British Columbia, Canada and the Pacific Northwest, U.S.A.

The Company sells to both foreign and domestic markets as follows:

	3 months June 30, 2006	3 months June 30, 2005	6 months June 30, 2006	6 months June 30, 2005
Canada	\$ 65,830	\$ 64,163	\$ 118,623	\$ 116,716
United States	123,368	113,568	252,354	205,089
Japan	17,777	16,857	33,158	43,896
Other export	16,932	18,820	33,375	40,633
	\$ 223,907	\$ 213,408	\$ 437,510	\$ 406,334

Sales by product line are as follows:

	3 months June 30, 2006	3 months June 30, 2005	6 months June 30, 2006	6 months June 30, 2005
Lumber	\$ 173,532	\$ 161,812	\$ 351,200	\$ 323,906
Logs	21,396	30,425	36,001	47,783
Wood chips and other by products	9,340	8,282	18,434	16,494
Other	19,639	12,889	31,875	18,151
	\$ 223,907	\$ 213,408	\$ 437,510	\$ 406,334

The Company has capital assets, goodwill and other intangible assets located in:

	June 30, 2006	Dec. 31, 2005	June 30, 2005
Canada	\$ 205,548	\$ 214,211	\$ 238,160
United States	148,960	143,085	140,597
	\$ 354,508	\$ 357,296	\$ 378,757

### 11. Contingencies:

On May 16, 2002, the U.S. International Trade Commission ("USITC") published its final written determination on injury in the countervailing duty ("CVD") and antidumping duty ("ADD") investigations and stated that Canadian softwood lumber threatens material injury to the U.S. industry. As a result, effective from May 22, 2002, cash deposits were required for shipments at the rates determined by the U.S. Department of Commerce ("USDOC").

Effective December 12, 2005, the USDOC implemented new deposit rates based on its second Administrative review period (April 1, 2003 to March 31, 2004 for the CVD case; and May 1, 2003 to April 30, 2004 for the ADD case) and reduced the CVD deposit rate to 8.70% and the all others ADD rate to 2.11%. Effective January 23, 2006, the USDOC further amended the ADD rate to 2.10%, reducing the Company's combined CVD and ADD deposit rate to 10.80%. The Company has not recorded any receivable for prior periods related to the change in the cash deposit rate applicable to new shipments.

On November 23, 2005 Interfor was selected by the U.S. Department of Commerce ("USDOC") as a mandatory respondent in the third administrative review of the antidumping duty order on softwood lumber products from Canada ("ADD AR3"). As a mandatory respondent, the U.S. Department of Commerce ("USDOC") will calculate a company-specific ADD for the review period May 1, 2004 to April 30, 2005. In June the USDOC released a Notice of Preliminary Results of the Review which indicated Interfor's ADD rate would be 6.46%. The Company will be disputing the USDOC preliminary findings with respect to USDOC clerical errors and calculation methodology. The ADD AR3 is expected to be completed in late 2006 at which time Interfor will be assigned a final Company-specific ADD rate for the review period. This rate will also remain effective as a deposit rate for the Company until the release of the final results of the Fourth Administrative Review in late 2007.

The Company has expensed \$10,574,000 (2005 - \$14,899,000) in duties for the six months ended June 30, 2006. The Company has paid US\$101,590,000 in cash deposits since May 22, 2002. These total U.S. deposits translated at the June 30, 2006 exchange rate equate to \$113,395,000.

Interfor and other Canadian forest product companies, the Federal Government and Canadian provincial governments (together, "Canadian Interests") categorically deny U.S. allegations which result in the imposition of the CVD and ADD. While exploring the possibility of a negotiated settlement to the dispute, Canadian Interests continue to pursue appeals of the final CVD and ADD determinations with the appropriate courts, NAFTA panels and the World Trade Organization. As such, the actual amount of duties for softwood lumber products shipped will depend upon the outcome of these various appeals or upon a negotiated settlement.

## INTERNATIONAL FOREST PRODUCTS LIMITED

Notes to Unaudited Interim Consolidated Financial Statements

(Tabular amounts expressed in thousands except per share amounts)

Three and six months ended June 30, 2006 and 2005 (unaudited)

### 11. Contingencies (continued):

On April 27, 2006 the federal governments of Canada and the United States reached a framework agreement to resolve the softwood lumber dispute. On July 1, 2006 Canada and the United States agreed on the legal text of the agreement. The proposed agreement provides for the return of approximately 80% of duties paid, plus interest. The agreement has a term of seven years and provides for an extension of two years and for early termination by either government after two years. Canadian softwood lumber exporters will pay an export charge when the price of lumber is at or below US\$355 per thousand board feet, as determined by the Random Lengths Framing Lumber Composite Price. The Province of B.C. will have the right to choose between an export charge only or a lower export charge with a quota. This choice will be made separately for the B.C. Coast and B.C. Interior regions. A significant number of Canadian forest product companies and provincial governments have indicated that unless certain changes are made to the agreement they may not support the agreement and may refuse to withdraw their legal challenges. As of the date of this report it is not possible to determine whether a final settlement will be reached and whether the terms of the potential agreement will be varied.

### 12. Employee future benefits:

The total benefits cost under the Company's various pension plans (described in the Company's audited annual consolidated financial statements) are as follows:

	3 months June 30, 2006	3 months June 30, 2005	6 months June 30, 2006	6 months June 30, 2005
Defined contribution plan	\$ 364	\$ 431	\$ 839	\$ 911
Defined benefit plan	117	125	243	271
Unionized employees' pension plan	1,101	1,070	2,122	2,178
U.S. employees benefit plan	150	170	334	313
Senior management supplementary pension plan	22	157	112	235
Total pension expense	\$ 1,754	\$ 1,953	\$ 3,650	\$ 3,908

### 13. Financial instruments:

#### (a) Fair value of financial instruments:

At June 30, 2006, the fair value of the Company's long-term debt approximated its carrying value of \$39,067,000 as the long-term debt bears interest at current market rates. The fair values of other financial instruments approximate their carrying values due to their short-term nature.

#### (b) Derivative financial instruments:

The Company employs financial instruments, such as interest rate swaps and foreign currency forward and option contracts, to manage exposure to fluctuations in interest rates and foreign exchange rates. The Company does not expect any credit losses in the event of non-performance by counter parties as the counter parties are the Company's bankers.

As at June 30, 2006, the Company has outstanding obligations to sell a maximum of US\$10,500,000 at an average rate of CAD\$1.1220 and Japanese ¥380,000,000 at an average rate of ¥98.52 to the CAD\$1.00 during 2006. All foreign currency gains or losses to June 30, 2006 have been recognized in the Statement of Operations.

In September 2005, the Company entered into a cross currency interest rate swap. The Company swapped a notional \$20,000,000 USD denominated debt at an exchange rate of 1.1765 (CAD\$23,530,000). The Company will pay 5.84%, including a spread of 200 basis points, on the Canadian dollar equivalent and receive 90 day LIBOR plus a spread of 200 basis points on the US\$20,000,000. LIBOR will be recalculated at set interval dates. The swap will mature on September 1, 2009 and has been marked to market with all gains or losses recognized in the Statement of Operations.

#### (c) Sale of receivables:

During 2000, the Company entered into an agreement to sell designated trade receivables, with limited recourse, to a Trust. As these trade receivables are collected, they are replaced by new receivables to maintain the aggregate outstanding balance. In the first quarter, 2006, the Company renewed this agreement and extended its termination date to March 31, 2007. At June 30, 2006, the Company received cash proceeds of \$20,000,000 (June 30, 2005 - \$25,000,000), from the sale of receivables. Effective July 17, 2006, the Company temporarily reduced its sale of receivables to nil.



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