



# **FORTRESS PAPER LTD**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

**FOR THE THREE AND NINE MONTHS ENDED  
SEPTEMBER 30, 2017**



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**FORTRESS PAPER LTD.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**

This Management's Discussion and Analysis ("MD&A") of the financial condition and results of operations of Fortress Paper Ltd. ("we", "our", "us", "Fortress" or the "Company") is dated and has been prepared based on information available as at November 8, 2017. The MD&A should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto for the three and nine month periods ended September 30, 2017 (available on SEDAR at [www.sedar.com](http://www.sedar.com)). This MD&A provides a review of the significant developments that have impacted the Company's performance during the quarter ended September 30, 2017 relative to the previous quarter and prior year comparative quarter. The financial information contained herein has been prepared in accordance with International Accounting Standards ("IAS") 34 – Interim Financial Reporting as issued by the International Accounting Standards Board ("IASB").

This MD&A contains certain forward-looking information that reflects the current views and/or expectations of the Company with respect to its expectations, beliefs, assumptions, estimates and forecasts about its business and the industries and markets in which it operates. The reader is cautioned that statements comprising forward-looking information are not guarantees of future performance and involve known and unknown risks, uncertainties, assumptions and other factors which are difficult to predict and that may cause actual results or events to differ materially from those anticipated in such forward-looking information. Accordingly, readers should not place undue reliance on forward-looking information. Examples of such forward-looking information that may be contained in this document include statements regarding: growth and future prospects of our business; market conditions for dissolving pulp, viscose staple fibre, security papers and other products; benefits that may accrue to the Company as a result of certain acquisitions, dispositions, capital expenditure programs, equipment upgrades and maintenance shutdowns; expected operational performance figures, including costs, utilization rates and efficiencies; expected returns on certain business segments; expected shipment dates to new customers at the Landqart mill; possible elimination of anti-dumping duties; expectation on continuity of current order book at the Landqart mill; availability of funds for debt allocation; our perceptions of the industry and markets in which we operate and anticipated trends in such markets and in the countries in which we do business; the securing of new purchase orders for our products; and the anticipated benefits for programs and initiatives.

Assumptions underlying the Company's expectations regarding forward-looking information contained in this MD&A include, among others: that the Company will be able to effectively market its products; the ability of the Company to realize significant cost-savings from production improvements and cost reduction initiatives; that demand for viscose staple fibre will continue to grow which will result in an increased demand for dissolving pulp; that the Landqart mill will continue operating on a consistent and regular basis in order to produce and deliver on its banknote orders; that the cogeneration facility will continue operating on a consistent and regular basis; that the Landqart mill will be successful in securing new orders; the general stability of the economic, political and regulatory environments within the countries where the Company conducts operations; that the Company will be able to enter into enforceable supply agreements for dissolving pulp on favourable terms and diversify its customer base; the ability of the Company to obtain financing (if necessary) on acceptable terms; that interest and foreign exchange rates will not vary materially from current levels; and that our equipment will operate at expected levels.

Persons reading this MD&A are cautioned that statements comprising forward-looking information are only predictions, and that the Company's actual future results or performance are subject to certain risks and uncertainties including, without limitation: those relating to potential disruptions to production and delivery, including as a result of equipment failures, labour issues, the complex integration of processes and equipment and other factors; fluctuations in the market price for products sold; trade restrictions or import duties imposed by foreign governments; that the Company will not be able to meet its equipment repair targets; that the Company's continuing efforts to reverse the dissolving pulp antidumping duty will not be successful; failure to meet regulatory requirements; changes in the market; potential downturns in economic conditions; fluctuations in the price and supply of required materials; foreign exchange fluctuations; availability of financing (as necessary); dependence on major customers; and other risk factors detailed in our filings with the Canadian securities regulatory authorities. These risks, as well as others, could cause actual results and events to vary significantly. The Company does not

undertake any obligation to update any forward-looking information, except as required by applicable securities law.

Throughout this discussion, reference is made to “operating EBITDA”, defined as net income before interest, income taxes, depreciation, amortization, non-operating income and expenses and stock-based compensation, which the Company considers to be an indicative measure of operating performance and a metric to evaluate profitability. Reference is also made to “adjusted net loss”, calculated as net loss less specific items affecting comparability with prior periods and “adjusted net loss per share”, calculated as adjusted net loss divided by the weighted average number of shares outstanding in the period. Operating EBITDA, adjusted net loss and adjusted net loss per share are not generally accepted earnings measures and should not be considered as an alternative to net income (loss) or cash flows as determined in accordance with IFRS. As there is no standardized method of calculating these measures, the Company’s operating EBITDA, adjusted net loss and adjusted net loss per share may not be directly comparable with similarly titled measures used by other companies. Reconciliations of operating EBITDA and adjusted net loss to net income (loss) reported in accordance with IFRS and, on a segmented basis, operating income (loss) are included in this MD&A.

All references in this MD&A to “dollars” or “\$” are to Canadian dollars, “€” are to the euro currency unit, “CHF” are to Swiss francs and “US\$” are to United States dollars.

Market and industry data contained in this MD&A is based upon information, surveys or studies conducted by independent third parties and independent industry or general publications and the Company's knowledge of, and experience in, the markets in which it operates. The Company has no reason to believe that such information is false or misleading in any material respect, however market and industry data is subject to variation and cannot be verified with complete certainty due to limits on the availability and reliability of raw data, the voluntary nature of the data gathering process and other limitations and uncertainties inherent in any statistical survey. This information has not been independently verified by the Company, any of its respective directors, officers or representatives or any other person involved in the preparation of the MD&A and no representation is given as to the accuracy of any of the data referred to in this MD&A obtained from third party sources.

Where we disclose production costs in this MD&A, such costs are calculated based on a variety of factors and inputs which may result in such costs not being comparable to similar types of costs disclosed by other issuers.

## **Description of Business**

The Company was incorporated on May 30, 2006 under the laws of the Province of British Columbia. During the quarter ended September 30, 2017, the Company operated internationally in two distinct business segments: the Dissolving Pulp Segment and the Security Paper Products Segment.

The Company operates its dissolving pulp business through the Fortress Specialty Cellulose (“FSC”) mill located in Thurso, Québec, Canada, that also operates in the renewable energy generation sector through its cogeneration facility. The Company operates its security paper products business through the Landqart mill located in Switzerland, where it produces banknote, passport, visa and other brand protection and security papers. The segmentation of the Company's manufacturing operations is based on a number of factors, including production, production processes, and economic characteristics. Consistent with the Company’s overall strategy, we continue to explore various shareholder enhancing opportunities, including investments in industries external to the Company’s current business segments, as well as joint venture, partnership and divestiture transactions. The Company’s core strengths involve identifying and capitalizing on investment opportunities and divestitures. In relation to these core strengths, the Company may pursue opportunities outside of the Company’s existing business segments that would diversify the asset base or monetize existing assets.

## **Overall Performance**

Operating EBITDA was \$0.2 million for the three months ended September 30, 2017, a decrease of \$7.4 million versus the prior year comparative period and a decrease of \$4.1 million over the previous quarter. The Dissolving Pulp Segment and the Security Paper Products Segment generated operating EBITDA loss of \$0.5 million and operating EBITDA of \$1.8 million, respectively, and corporate costs were \$1.1 million in the third quarter of 2017.

The Company reported a net loss of \$14.3 million or basic and diluted net loss per share of \$1.00 for the third quarter of 2017. In the second quarter of 2017, the Company reported net loss of \$2.1 million or basic and diluted net loss per share of \$0.15. For the third quarter of 2016, the Company reported a net income of \$20.3 million or basic and diluted net income per share of \$1.38 and \$1.34, respectively.

The Dissolving Pulp Segment generated operating EBITDA loss of \$0.5 million for the quarter ended September 30, 2017, representing a decrease of \$4.0 million compared to the second quarter of 2017 and a decrease of \$12.4 million compared to the prior year comparative period. An operating cost adjustment of \$2.6 million representing labor and associated overhead incurred during the previously reported auxiliary system failure and consequent 11 days of lost production in September have been adjusted out of operating EBITDA (See "Significant Developments – Auxiliary System Failure at the FSC Mill"). This amount does not represent the totality of the insurance claim. The results of the third quarter of 2017 were also negatively impacted by approximately 5% lower realized sales prices, a stronger Canadian dollar relative to the US dollar and higher costs associated with the previously mentioned evaporation bottleneck which is scheduled to be permanently remediated during the fourth quarter annual planned shutdown. In addition to the foregoing, a two day planned shutdown, also impacted results. A total of 28,870 air dried metric tonnes ("ADMT") of dissolving pulp were produced in the third quarter of 2017. During the quarter ended September 30, 2017, the FSC mill sold 32,048 ADMT of dissolving pulp compared to 34,672 ADMT and 40,992 ADMT in the previous quarter and prior year comparative period, respectively.

In the third quarter of 2017, the FSC mill's production costs, including amortization of some of the shutdown costs and the positive impact of the cogeneration facility, averaged \$1,008 per ADMT after adjusting for the impact of the unplanned shut down. Production costs in the second quarter of 2017 and prior year comparative period averaged \$991 and \$787 per ADMT, respectively.

The Security Paper Products Segment results were slightly better than expected and generated operating EBITDA of \$1.8 million for the third quarter of 2017, a decrease of \$1.0 million when compared to the second quarter of 2017, and a \$3.6 million increase when compared to results in the third quarter of 2016. Results for the third quarter of 2017 were primarily impacted by a decrease in shipments due to timing and product mix compared to the previous quarter. Relative to the prior year comparative period, the third quarter of 2017 saw improved production efficiencies, product mix and waste rates. The build-out and installation of the second finishing machine has been completed and is operational. The additional finishing machine is expected to debottleneck the mill and provide more production flexibility. The Landqart mill sold 1,911 tonnes of security paper in the third quarter of 2017, compared to 3,139 and 2,431 tonnes of security paper in the second quarter of 2017 and third quarter of 2016, respectively. Security paper production includes banknotes and passports, which result in varying degrees of costs and margins depending on the complexity of the security features included.

## **Management's Outlook**

### ***Dissolving Pulp Segment***

The Company completed the necessary repairs at the FSC mill caused by the failure of a pressurized auxiliary gas collection system which occurred on September 20, 2017 and re-commenced production of dissolving pulp on October 6, 2017. Production and the cogeneration facility have since been operating in the ordinary course. The failure was an unforeseen event, for which the team at the FSC mill responded with tireless effort in resolving the system failure and achieving a restart three days earlier than anticipated.

To address the production challenges experienced in the second and third quarters of 2017, corrective measures and efficiency initiatives have been identified and scheduled to be completed during the annual November

shutdown. One component of the previously announced Birch and Hemicellulose Project is expected to permanently rectify the primary operational challenge experienced during the second and third quarters in the chemical recovery area. This phase of the project is to be completed during the annual shutdown in the fourth quarter of 2017. The shutdown is planned to be 8 days in November.

Further, the fifth digester project, scheduled to be completed in the first quarter of 2018, is expected to result in an incremental annual production capacity increase of 8,500 ADMT in 2018 and 17,000 ADMT in 2019 compared to current production capacity.

Dissolving pulp pricing was strong through the early part of 2017 reaching a high of US \$960 per ADMT before reducing in June 2017 due primarily to a temporary build up in viscose staple fibre (“VSF”) and yarn inventory levels, a drop in cotton linter prices and an increase in exports to China from an Indonesian pulp producer. However, dissolving pulp prices have gradually increased to the current price of approximately US \$930 per ADMT.

VSF prices have softened in the past three weeks but, year to date on a weekly average, remain US \$249 per ADMT above the 2016 comparative period. VSF price is also supported by improved cotton pricing over the past two years. Chinese Spot cotton pricing is currently up over 5% year over year. Reserve cotton sales for 2017 ran from March through September 2017, further reducing the large Chinese stockpile which is expected to improve stability in the cotton market. Ending stocks in China for 2017/2018 are projected to decline more than 18.4% to 39.5 million bales, the lowest level in six years. The supply of higher quality imported cotton remains limited. The decline in forecasted cotton production and the limited availability of higher quality cotton stocks continue to reinforce the shift to manmade materials, which has resulted in increased demand and price increases for textile feedstocks including VSF.

In the fourth quarter, management expects that there will be further adjustments to EBITDA related to the production ramp up subsequent to the FSC mill restart after the auxiliary failure and related insurance recovery accrual. After the adjustment, EBITDA at Thurso is expected to slightly improve compared to the third quarter despite the planned annual shutdown in November.

### ***Security Paper Products Segment***

The Landqart mill has received notices from one of its significant international customers cancelling that portion of purchase orders which were scheduled for production and delivery by the Landqart mill in the fourth quarter of 2017 and in fiscal 2018. The cancelled purchase orders represent approximately 16% of the budgeted order book at the Landqart mill for fiscal 2017 and 30% for fiscal 2018. Despite other suppliers experiencing similar cancellations, Landqart continues to have dialogue with the customer to potentially reinstate all or a portion of the cancelled orders over an extended period of time within fiscal 2018. There are no assurances that any reinstatement will be forthcoming.

Management is seeking to fill the production void caused by the cancellations and is deploying various strategies, including: (a) pulling forward existing purchase orders, (b) seeking new orders from existing and new customers, and (c) requesting special one-time supplemental orders from existing customers for immediate production. It is expected that revenues will be negatively impacted in the fourth quarter of 2017 as the decline in anticipated production volume is unlikely to be replaced in its entirety in the short term. Given the relatively long sales cycle for banknote papers, the reduced banknote production in the fourth quarter will also have an impact on revenues and results in the first quarter of 2018. Management is working diligently to replenish the majority of the order book in a timely manner. However, there is no assurance that such efforts will be successful, in which case the Landqart mill may be required to take market downtime on certain aspects of its operations. Other strategies are also being evaluated in order to mitigate the financial impact and potential legal remedies are being assessed.

Production of Durasafe® for the substrate of the ninth series of the Swiss franc for the Swiss National Bank (“SNB”) began in 2014 and will continue for all series expected through to 2019. The SNB issued the new 50 franc note in April 2016, the 20 franc note in May 2017 and the 10 franc note in October 2017, all printed on Durasafe®. These are the first three of six notes in the SNB ninth series. In March 2016, the National Bank of

Kazakhstan 20,000 Tenge banknote produced with Durasafe® banknote substrate was the recipient of the Regional Banknote of the Year award at the High Security Printing Europe conference. In April 2017, the Swiss 50 Franc was the recipient of the International Bank Note Society 2016 bank note of the year award. Based on multiple Durasafe® trials being conducted at various stages, management continues to anticipate additional orders in the near, medium and long term. In June 2017, the Central Bank of the Bahamas chose Durasafe® for the two highest denominations of its “Crisp Evolution” Series.

The global market for security paper is growing. Specifically, demand for banknote currency is increasing globally and is expected to remain a significant method of payment in the foreseeable future.

Assuming non-replacement of the previously announced order cancellation at Landqart, operating results will be lower as compared to the third quarter. Management is still working on multiple avenues to replace this lost order, though there can be no assurance how much, if any, of this order can be replaced in the short term.

## **Significant Developments**

### ***Retirement of Yvon Pelletier***

Effective October 1, 2017, Mr. Yvon Pelletier retired as President and Chief Executive Officer of the Company after serving in this capacity for two years. Previously, Mr. Pelletier served as President of the Company's dissolving pulp business from February 2013 until October 2015. Under Mr. Pelletier's leadership, the Company experienced notable operational and financial improvements, and completed several significant transactions and financings. Mr. Pelletier will continue providing consulting services to the Company for up to two years in order to assist the Company in its transition subsequent to his departure. Mr. Chadwick Wasilenkoff replaced Mr. Pelletier as President and Chief Executive Officer of the Company.

### ***Auxiliary System Failure at the FSC Mill***

On September 21, 2017, the Company announced that there was a burst in a pressurized auxiliary gas collection system relating to one of the recovery boilers at the FSC mill. There were no injuries or material damage to property or environmental impact. The Company completed the necessary repairs at the FSC mill caused by the failure of the pressurized auxiliary gas collection system and re-commenced production of dissolving pulp on October 6, 2017.

The Company has initiated an insurance claim pursuant to its property damage and business interruption insurance coverage, which has a \$2.5 million deductible. Receipt of insurance proceeds has not been recorded in the financial statements, as the recognition criteria under IFRS have not yet been met.

### ***Landqart Mill Order Cancellation***

The Landqart mill has received notices from one of its significant international customers cancelling that portion of purchase orders which were scheduled for production and delivery by the Landqart mill in the fourth quarter of 2017 and in fiscal 2018. These cancelled orders represent approximately 16% of the budgeted order book at the Landqart mill for fiscal 2017 and 30% for fiscal 2018 (see “Management's Outlook – Security Paper Products Segment”).

## Selected Quarterly Information

(thousands of dollars, except per share amounts and foreign exchange rates, unaudited)

	Q3 2017	Q2 2017	Q1 2017	Q4 2016
Sales	65,066	86,599	92,460	80,863
Net loss	(14,319)	(2,087)	(2,745)	(7,274)
Basic and diluted net loss per share	(1.00)	(0.15)	(\$0.19)	(\$0.51)
Weighted average shares outstanding – Basic	14,273	14,307	14,311	14,184
Weighted average shares outstanding – Diluted	14,273	14,307	14,311	14,184
Average Swiss franc/Canadian dollar exchange rate <sup>(1)</sup>	1.3012	1.3664	1.3194	1.3327
Average US\$/Canadian dollar exchange rate <sup>(1)</sup>	1.2528	1.3450	1.3238	1.3341

<sup>(1)</sup> Source – Bank of Canada (average noon rate for the period)

(thousands of dollars, except per share amounts and foreign exchange rates, unaudited)

	Q3 2016	Q2 2016	Q1 2016	Q4 2015
Sales	82,148	87,993	80,012	74,576
Net income (loss)	20,301	6,893	(13,041)	(3,680)
Basic net income (loss) per share	\$1.38	\$0.47	(\$0.88)	(\$0.25)
Diluted net income (loss) per share	\$1.34	\$0.45	(\$0.88)	(\$0.25)
Weighted average shares outstanding – Basic	14,748	14,812	14,803	14,727
Weighted average shares outstanding – Diluted	15,149	15,205	14,803	14,727
Average Swiss franc/Canadian dollar exchange rate <sup>(1)</sup>	1.3376	1.3281	1.3819	1.3474
Average US\$/Canadian dollar exchange rate <sup>(1)</sup>	1.3050	1.2886	1.3732	1.3354

<sup>(1)</sup> Source – Bank of Canada (average noon rate for the period)

## Historical Discussion

The FSC mill recorded positive operating EBITDA in 2015, as a result of increased production, improved costs and increased dissolving pulp and electricity sales. Following the annual maintenance shutdown in the fourth quarter of 2015, the FSC mill experienced a challenging restart period. The fixed costs incurred during the shutdown, combined with the impact of the lime kiln repair, had a negative impact on the fourth quarter of 2015. The first quarter of 2016 saw improved pricing for dissolving pulp, continued stable electricity generation and favourable foreign exchange rates on sales primarily denominated in US\$, offset by a ten day shutdown due to a blockage issue in the mill and limitations in digester capacity. The fixed costs incurred during the shutdown had a negative impact on first quarter costs in the amount of \$2.5 million. The second quarter of 2016 results improved due to increased productivity and continued stable electricity generation. The third quarter saw improved productivity and production costs, continued stable electricity generation and improved pricing. The fourth quarter of 2016 was impacted by the planned annual maintenance shutdown. The results of the first quarter of 2017 were positively impacted by improvements in production rates and quality, particularly during the normally slower winter season, as well as better pricing relative to the prior year comparative period. The second quarter of 2017 was negatively impacted by operational challenges in the chemical recovery area of the mill. The third quarter of 2017 was negatively impacted by the continuing challenges in the chemical recovery area and an auxiliary system failure during the third quarter at the FSC mill which caused the mill to temporarily suspend the production of dissolving pulp in order to complete the necessary repairs (See “Significant Developments – Auxiliary System Failure at the FSC Mill”).

The year ended December 31, 2015 was characterized by a favourable product mix and increased improvements in efficiency and waste rates at the Landqart mill, partially offset by the significant appreciation of the Swiss franc against the euro. The first half of 2016 was favourably impacted by product mix. The second half of 2016 was

impacted by unfavourable product mix and technical challenges that led to mill inefficiencies. Results at the Landqart mill for the first half of 2017 were higher than the second half of 2016, due primarily to a more favourable product mix and reduced waste rates after technical challenges were resolved. Results for the third quarter of 2017 were impacted by lower shipments when comparing to the second quarter of 2017.

### Third Quarter 2017 Earnings Review

#### Three Months Ended September 30, 2017

##### Overview

Operating EBITDA was \$0.2 million for the three months ended September 30, 2017. For the three months ended June 30, 2017, operating EBITDA was \$4.3 million and for the three months ended September 30, 2016, operating EBITDA was \$7.6 million. The Dissolving Pulp Segment generated operating EBITDA loss of \$0.5 million and the Security Paper Products Segment generated operating EBITDA of \$1.8 million. Corporate costs contributed an operating EBITDA loss of \$1.1 million in the third quarter of 2017.

The Company reported a net loss of \$14.3 million or basic and diluted net loss per share of \$1.00 for the third quarter of 2017. In the second quarter of 2017, the Company reported net loss of \$2.1 million or basic and diluted net loss per share of \$0.15. For the third quarter of 2016, the Company reported net income of \$20.3 million or basic and diluted net income per share of \$1.38 and \$1.34, respectively.

Fortress reported an adjusted net loss of \$15.1 million or basic and diluted adjusted net loss per share of \$1.05 for the third quarter of 2017 on sales of \$65.1 million. In the second quarter of 2017, the Company reported an adjusted net loss of \$8.2 million, or basic and diluted adjusted net loss per share of \$0.57 on sales of \$86.6 million, and for the third quarter of 2016, an adjusted net loss of \$3.8 million or basic and diluted adjusted net loss per share of \$0.26 on sales of \$82.1 million.

Manufacturing and distribution costs were \$58.8 million, or 90.3% of sales, for the three months ended September 30, 2017, compared to \$71.0 million, or 81.9%, for the three months ended June 30, 2017. In the third quarter of 2016, manufacturing and distribution costs were \$62.2 million, or 75.8% of sales. Such costs are representative of tonnage sold and production cost per tonne at each mill.

SG&A expenses were \$8.7 million for the third quarter of 2017, compared to \$11.9 million for the second quarter of 2017. The prior year comparative period SG&A was \$12.3 million. SG&A was lower in the third quarter of 2017 compared to the second quarter of 2017 and prior year comparative quarter due primarily to a reduction in variable compensation accruals related to company performance and lower sales costs.

#### Selected Financial Information and Statistics

(thousands of dollars, except shipments, unaudited)	Q3 2017	Q2 2017	Q3 2016
Sales	65,066	86,599	82,148
Operating EBITDA <sup>(1)</sup>	202	4,289	7,628
Net (loss) income	(14,319)	(2,087)	20,301
Adjusted net loss <sup>(2)</sup>	(15,053)	(8,193)	(3,847)
Paper shipments (tonnes)	1,911	3,139	2,431
Pulp shipments (ADMT)	32,048	34,672	40,992

<sup>(1)</sup> See Net (Loss) Income to Operating EBITDA Reconciliation.

<sup>(2)</sup> See Net (Loss) Income to Adjusted Net Loss Reconciliation.

**Net (Loss) Income to Adjusted Net Loss Reconciliation:**

(thousands of dollars, except per share amounts, unaudited)	Q3 2017	Q2 2017	Q3 2016
Net (loss) income	(14,319)	(2,087)	20,301
Foreign exchange (gain) loss	(757)	(3,907)	474
Reversal of legal provision	-	(2,731)	-
Nonrecurring salary adjustment	-	540	-
Loss (gain) on disposal of assets	23	(8)	(24,622)
Adjusted net loss	(15,053)	(8,193)	(3,847)
Basic net (loss) income per share	(1.00)	(0.15)	1.38
Diluted net (loss) income per share	(1.00)	(0.15)	1.34
Adjusted net loss per share, basic and diluted	(1.05)	(0.57)	(0.26)

**Net (Loss) Income to Operating EBITDA Reconciliation:**

(thousands of dollars, unaudited)	Q3 2017	Q2 2017	Q3 2016
Net (loss) income	(14,319)	(2,087)	20,301
Income tax recovery	(4)	(17)	-
Foreign exchange (gain) loss	(757)	(3,907)	474
Net finance expense	4,051	4,064	3,918
Amortization	8,685	8,586	7,522
Loss (gain) on disposal of assets	23	(8)	(24,622)
Gain on financial instruments	(348)	(427)	(32)
Stock-based compensation	280	276	67
Auxiliary system failure	2,591	-	-
Reversal of legal provision	-	(2,731)	-
Non-recurring salary adjustment	-	540	-
Operating EBITDA	202	4,289	7,628

**Operating Results by Business Segment**

*Dissolving Pulp Segment*

(thousands of dollars, except for shipments, unaudited)	Q3 2017	Q2 2017	Q3 2016
Sales	35,299	42,808	48,862
Operating (loss) income	(9,657)	(2,882)	6,465
Auxiliary system failure	2,591	-	-
Amortization	6,564	6,359	5,403
Operating EBITDA (loss)	(502)	3,477	11,868
Dissolving pulp shipments (ADMT)	32,048	34,672	40,992

The Dissolving Pulp Segment generated operating EBITDA loss of \$0.5 million for the quarter ended September 30, 2017, representing a decrease of \$4.0 million compared to the second quarter of 2017, and a decrease of \$12.4 million compared to the prior year comparative period. An operating cost adjustment of \$2.6 million represents labor and associated overhead incurred during the previously reported auxiliary system failure and consequent 11 days of lost production in September have been adjusted out of operating EBITDA (See "Significant Developments – Auxiliary System Failure at the FSC Mill), however; this amount does not represent the totality of the insurance

claim. The results of the third quarter of 2017 were also negatively impacted by approximately 5% lower realized sales prices, a stronger Canadian dollar relative to the US dollar and higher costs associated with the previously mentioned evaporation bottleneck which remains slated to be permanently remediated during the fourth quarter shut. In addition to the foregoing, a two day planned outage, also impacted results. A total of 28,870 ADMT of dissolving pulp were produced in the third quarter of 2017. During the quarter ended September 30, 2017, the FSC mill sold 32,048 ADMT of dissolving pulp compared to 34,672 ADMT and 40,992 ADMT in the previous quarter and prior year comparative period, respectively.

Revenues of \$4.7 million were generated from the cogeneration facility in the quarter ended September 30, 2017 compared to \$5.3 million in the quarter ended June 30, 2017. The decrease in quarter three revenue compared to second quarter revenue is primarily related to the auxiliary system failure (See "Significant Developments – Auxiliary System Failure at the FSC Mill") which resulted in the cogeneration facility operating at a reduced rate for a temporary period. Revenues from the generation of power at the cogeneration facility during the quarter ended September 30, 2016 were \$5.6 million.

As at September 30, 2017, the FSC mill held finished goods inventory consisting of 634 ADMT of dissolving pulp compared to 3,812 ADMT as at June 30, 2017. At September 30, 2016, the mill held finished goods inventory consisting of 988 ADMT of dissolving pulp.

#### *Security Paper Products Segment*

(thousands of dollars, except for shipments, unaudited)	Q3 2017	Q2 2017	Q3 2016
Sales	29,767	43,791	33,286
Operating income (loss)	(339)	54	(3,921)
Non-recurring salary adjustment	-	540	-
Amortization	2,121	2,227	2,119
Operating EBITDA (loss)	1,782	2,821	(1,802)
Shipments (tonnes)	1,911	3,139	2,431

The Security Paper Products Segment results were slightly better than expected and generated operating EBITDA of \$1.8 million for the third quarter of 2017, a decrease of \$1.0 million when compared to the second quarter of 2017, and a \$3.6 million increase when compared to results in the third quarter of 2016. Results for the third quarter of 2017 were primarily impacted by a decrease in shipments due to timing and product mix compared to the previous quarter. Relative to the prior year comparative period, the third quarter of 2017 saw improved production efficiencies, product mix and waste rates. Relative to the prior year, the third quarter of 2017 saw improved production efficiencies, product mix and waste rates. The Landqart mill sold 1,911 tonnes of security paper in the third quarter of 2017, compared to 3,139 and 2,431 tonnes of security paper in the second quarter of 2017 and third quarter of 2016, respectively. Security paper production includes banknotes and passports, which result in varying degrees of costs and margins depending on the complexity of the security features included. In July 2017, a product claim in the Security Paper Products Segment dating back to July 2012 was dismissed by the courts and a \$2.7 million reversal of a legal provision was recorded.

***Nine Months Ended September 30, 2017***

***Selected Financial Information and Statistics for the Nine Months Ended:***

(thousands of dollars, except for shipments, unaudited)	<b>September 30, 2017</b>	<b>September 30, 2016</b>
Sales	244,125	250,153
Operating EBITDA <sup>(1)</sup>	11,980	14,990
Net (loss) income	(19,151)	14,153
Adjusted net loss <sup>(2)</sup>	(26,245)	(22,957)
Paper shipments (tonnes)	7,886	7,800
Pulp shipments (ADMT)	104,553	112,685

<sup>(1)</sup> See Net (Loss) Income to Operating EBITDA Reconciliation.

<sup>(2)</sup> See Net (Loss) Income to Adjusted Net Loss Reconciliation.

***Net (Loss) Income to Adjusted Net Loss Reconciliation:***

(thousands of dollars, except per share amounts, unaudited)	<b>September 30, 2017</b>	<b>September 30, 2016</b>
Net (loss) income	(19,151)	14,153
Foreign exchange (gain) loss	(4,918)	1,887
Loss on disposal of assets	15	-
Reversal of legal provision	(2,731)	-
Nonrecurring salary adjustment	540	-
Gain on disposal of assets	-	(24,622)
Reversal of impairment of property, plant and equipment	-	(14,375)
Adjusted net loss	(26,245)	(22,957)
Basic net (loss) income per share	(1.34)	0.96
Diluted net (loss) income per share	(1.34)	0.93
Adjusted net loss per share, basic and diluted	(1.84)	(1.55)

## Net (Loss) Income to Operating EBITDA Reconciliation:

(thousands of dollars, unaudited)	September 30, 2017	September 30, 2016
Net (loss) income	(19,151)	14,153
Income tax	-	10
Foreign exchange (gain) loss	(4,918)	1,887
Net finance expense	9,961	14,326
Amortization	25,793	23,076
(Gain) loss on financial instruments	(801)	393
Stock based compensation	681	142
Auxiliary system failure	2,591	-
Reversal of legal provision	(2,731)	-
Non-recurring salary adjustment	540	-
Reversal of impairment of property, plant and equipment	-	(14,375)
Loss (gain) on disposal of assets	15	(24,622)
Operating EBITDA	11,980	14,990

### Overview

During the nine months ended September 30, 2017, the Company reported net loss of \$19.2 million or basic and diluted net loss per share of \$1.34. During the nine months ended September 30, 2016, the Company reported net income of \$14.2 million or basic and diluted net income per share of \$0.96 and \$0.93, respectively.

Operating EBITDA for the Company was \$12.0 million for the nine months ended September 30, 2017 on sales of \$244.1 million compared to operating EBITDA of \$15.0 million for the nine months ended September 30, 2016 on sales of \$250.2 million.

During the nine months ended September 30, 2017, the Dissolving Pulp Segment generated an operating EBITDA of approximately \$11.3 million compared to \$16.4 million operating EBITDA in the prior year comparative period. The Security Paper Products Segment generated operating EBITDA of \$6.1 million in the nine months ended September 30, 2017 compared to operating EBITDA of \$4.7 million in the prior year comparative period. Corporate costs contributed to operating EBITDA loss of \$5.4 million and \$6.1 million in the nine months ended September 30, 2017 and 2016, respectively.

Adjusted net loss for the nine months ended September 30, 2017, was \$26.2 million or \$1.84 per share basic and diluted. Adjusted net loss for the prior year comparative period was \$23.0 million or \$1.55 per share basic and diluted.

Manufacturing, product, freight and other distributions costs totaled \$201.9 million, or 82.7% of sales, for the nine months ended September 30, 2017, compared to \$198.2 million, or 79.2% of sales, for the nine months ended September 30, 2016. The increase in costs as a percentage of sales in 2017 primarily related to decreased tonnage shipped as well as increased costs per tonne at our FSC mill for the nine months to date.

SG&A expenses were \$33.3 million for the nine months ended September 30, 2017 compared to \$37.0 million for the prior year comparative period. SG&A was lower in the current year due primarily to a reduction in variable compensation accruals related to company performance and lower sales costs.

In July 2017, a product claim in the Security Paper Products Segment dating back to July 2012 was dismissed by the courts and a \$2.7 million reversal of a legal provision was recorded.

During the first nine months of 2016, the Company completed the sale of the buildings, equipment, ancillary property, and energy generation and transmission plant located in Lebel-sur-Quévillon, Québec, which closed in

July 2016. As a result of the sale, the Company recorded a \$14.4 million reversal of the impairment taken during the fourth quarter of 2013.

During the first nine months of 2016, the Company also completed the sale of its land and buildings relating to its security paper business for the aggregate purchase price of CHF 44.5 million and recorded a gain of \$24.6 million.

Stock-based compensation was \$0.7 million for the nine months ended September 30, 2017 compared to \$0.1 million in the prior year comparative period.

Foreign exchange gains and losses relate primarily to translation losses or gains on foreign denominated debt.

## Operating Results by Business Segment

### *Dissolving Pulp Segment*

(thousands of dollars, except for shipments, unaudited)	Nine Months Ended	
	September 30, 2017	September 30, 2016
Sales	126,797	131,443
Operating (loss) income	(10,634)	351
Auxiliary system failure	2,591	-
Amortization	19,325	16,025
Operating EBITDA	11,282	16,376
Dissolving Pulp Shipments (ADMT)	104,553	112,685

Operating EBITDA for the nine months ended September 30, 2017 at the FSC mill was \$5.1 million lower relative to the prior year comparative period primarily due to lower production volume and higher production costs. During the second and third quarters of 2017, results were impacted by operational challenges experienced in the chemical recovery area of the mill, as well as a planned outage that reduced production. At the end of the third quarter, an auxiliary system failure at the FSC mill (See "Significant developments – Auxiliary System Failure at the FSC Mill") caused the mill to temporarily suspend the production of dissolving pulp in order to complete the necessary repairs.

### *Security Paper Products Segment*

(thousands of dollars, except for shipments, unaudited)	Nine Months Ended	
	September 30, 2017	September 30, 2016
Sales	117,328	118,710
Operating loss	(937)	(2,339)
Non-recurring salary adjustment	540	-
Amortization	6,468	7,051
Operating EBITDA	6,071	4,712
Shipments (tonnes)	7,886	7,800

During the year ended December 31, 2016, the Company completed the sale of its land and buildings relating to its security paper business in the security paper products segment for the aggregate purchase price of CHF 44.5 million. As a result of the sale and leaseback transaction, rent of \$2.7 million was incurred in the first nine months of 2017 compared to \$0.9 million in the prior year comparative period.

### Selected Cash Flow Items

	Q3 2017	Q2 2017	Nine Months Ended September 30, 2017	Q3 2016	Nine Months Ended September 30, 2016
<b>Cash flows from (used by) operating activities</b>					
Cash from operating activities before working capital changes	(1,943)	4,385	10,526	7,415	15,612
Non-cash working capital change	2,667	4,859	14,873	957	(4,636)
	724	9,244	25,399	8,372	10,976
<b>Cash flows (used by) from financing activities</b>	(2,906)	(3,550)	4,881	(9,613)	(18,398)
<b>Cash flows (used by) from investing activities</b>					
Additions to property, plant and equipment	(10,033)	(9,705)	(26,684)	(3,930)	(13,528)
Other	850	8,845	8,015	56,522	66,152
	(9,183)	(860)	(18,669)	52,592	52,624
<b>Change in cash position</b>	(11,365)	4,834	11,611	51,351	45,202
Foreign exchange loss on cash and cash equivalents	(133)	77	123	384	(1,113)
Cash and cash equivalents, beginning of period	45,364	40,453	22,132	26,318	33,964
<b>Cash and cash equivalents, end of period</b>	<b>33,866</b>	<b>45,364</b>	<b>33,866</b>	<b>78,053</b>	<b>78,053</b>

### Operating Activities

Fortress operates in a cyclical industry and its operating cash flows vary accordingly. Fortress' principal operating cash expenditures are for labour and raw materials. Operating activities provided cash of \$25.4 million and \$11.0 million in the nine months ended September 30, 2017 and 2016, respectively. Working capital is subject to cyclical operating needs, with inventory usually at the lower end of the cycle during summer months. Collection of receivables is dependent on timing of finished goods shipments, while accounts payable typically peak at the end of the year.

### Financing Activities

During the first nine months of 2017, financing activities provided cash of \$4.9 million. Included in financing activities for the nine months ended September 30, 2017 was the repayment of a \$25.0 million unsecured convertible debenture. The Company also entered into an agreement with a new lender for a \$40.0 million secured loan (the "IAM Loan") and made \$3.1 million in long-term debt and \$7.0 million in interest payments. Pursuant to the Company's normal course issuer bid for common shares the Company repurchased 104,468 common shares for a total cost of \$0.6 million at an average price of \$5.95 per share during the second and third quarters of 2017.

During the first nine months of 2016, financing activities used cash of \$18.4 million. Included in financing activities for the nine months ended September 30, 2016, was \$3.0 million for the repurchase of common shares, \$9.2 million for the repurchase of convertible debt and \$6.2 million related to the payment of long-term debt interest and financing fees.

### ***Investing Activities***

Investing activities in the first nine months of 2017 used cash of \$18.7 million. Investing activities relating to the purchase of equipment and other capital expenditures at the mills used cash of \$26.7 million. Restricted cash provided cash of \$2.1 million. The Company received \$5.7 million in government grants relating to the fifth digester project.

Investing activities in the first nine months of 2016 provided cash of \$52.6 million. Investing activities relating to the purchase of equipment and other capital expenditures at the mills was \$13.5 million. Cash proceeds from the sale and lease back transaction at the Landqart mill provided cash of \$58.4 million. The Company received \$3.2 million for the sale of marketable securities. Restricted cash, relating to cash security provided primarily for banknote contracts in the Security Paper Products Segment, provided \$4.3 million in cash as performance bonds expired.

### **Liquidity and Capital Resources**

As at September 30, 2017, the Company had a cash and cash equivalents balance of \$33.9 million. Business maintenance capital expenditure was approximately \$5.9 million in the quarter ended September 30, 2017. Project and/or discretionary capital expenditure for the quarter ended September 30, 2017 was approximately \$3.2 million.

As at September 30, 2017, the Company had \$12.9 million in restricted cash. Included in the restricted cash balance was \$4.6 million (CHF 3.6 million) in rent and maintenance deposits as a result of the sale and leaseback transaction and a \$3.6 million deposit as a result of the IAM loan. The remaining balance is cash required for collateral on performance bonds.

At September 30, 2017, the Company's current portion of long-term debt, accounts payable and accrued liabilities totaled \$57.1 million, all of which fall due for payment within one year of the statement of financial position date. If necessary, the Company has the ability to repay principal amounts outstanding, subject to receiving requisite approvals, of the remaining \$62.1 million of convertible debentures due in 2019 in common shares of the Company. In February 2017, the Company repurchased in full the unsecured convertible debenture in the aggregate principal amount of \$25.0 million in favour of Fonds de solidarité FTQ that was set to mature on June 20, 2017.

Corporate expenses in the third quarter of 2017 decreased by \$0.9 to \$1.1 million compared to the previous quarter.

Cash and restricted cash ended the third quarter at \$46.7 million up from \$37.1 million at the 2016 fiscal year end. Although there can be no assurances, Fortress believes that current cash, cash generated from operations, cashflow derived from improved working capital management, cash from the sale of assets, alternative financing arrangements, and other cash generating initiatives, should be sufficient to meet its debt service, capital expenditure, short term working capital requirements, and investment activities external to the Company's current business segments. Fortress' future operating performance and its ability to finance capital expenditures, service its debt, repay its indebtedness upon maturity and pay other indebtedness will be subject to future economic conditions, the potential renegotiation or refinancing of existing indebtedness, the financial success of Fortress' business, Fortress' ability to successfully maximize margins and diversify product mix in response to changing market conditions, success of cost savings initiatives and other factors, some of which are not within Fortress' control, including but not limited to changes in market prices for its products, raw materials costs, foreign currency exchange rates and the impact of duties and tariffs. No assurances are given as to the likelihood that the outcome

of any such factors will be successful or will operate to positively impact the Company's business, operations and/or financial results.

Fortress may determine, in its sole discretion, that market or financial conditions may warrant that it seek additional sources of capital on terms satisfactory to Fortress, including, but not limited to additional debt or equity financing, in order to fund capital expenditures, refinance indebtedness, provide additional working capital, enhance liquidity or for other general corporate purposes.

In July 2016 the sale of the assets of the Fortress Global Cellulose mill was completed. The mill had previously been fully impaired for accounting purposes. Concurrent with the sale, the Company assigned and transferred a \$7.0 million note issued by the purchaser to Investissement Québec ("IQ") as early repayment of principal amounts due in 2017 under the IQ loan. In addition, IQ has agreed to defer interest on the IQ loan until April 1, 2018 and to further defer an aggregate of \$6.3 million of quarterly principal payments otherwise payable September 30, 2017, December 31, 2017, and March 31, 2018, without penalty or interest accruing on such amounts until the one year anniversary of each such principal payment due date. The remaining principal amount will be amortized in equal quarterly installments commencing June 30, 2018 over the remaining term of the loan. In connection with the IAM Loan, Fortress agreed to increase the interest payable on \$40.0 million principal amount of the IQ loan to 6% per annum and pay interest on this portion of the IQ loan commencing February 2017. All principal payments to IQ will be applied firstly to the higher interest bearing principal amount outstanding.

Repayments of principal for debt outstanding as at September 30, 2017 are required as follows:

	(\$ 000's)
2017	1,545
2018	13,078
2019	77,031
2020	14,860
2021	14,868
Thereafter	84,719
	206,101

As at September 30, 2017, the Company had \$68.1 million net working capital and aggregate indebtedness of \$211.8 million, including unamortized borrowing costs.

#### *Commitments*

As at September 30, 2017, the Company has:

- committed to purchase steam from a supplier up to the end of 2025 for \$1.2 million (CHF 0.9 million) per year;
- issued guaranteed letters of credit of \$0.8 million relating to the continued delivery of power at our cogeneration facility and a performance security guarantee of up to \$2.0 million for derivative financial instruments;
- guaranteed the secured note receivable transferred to a lender as early repayment of principal amounts due in 2017;
- committed to purchase \$8.7 million in property, plant and equipment; and
- performance bonds in the amount of \$24.5 million (EUR 16.6 million).

The remaining minimum operating lease commitments for land, buildings, equipment, storage, and offices over the next five years and thereafter are as follows:

	(\$ 000's)
2017	1,899
2018	4,302
2019	4,242
2020	3,917
2021	3,541
Thereafter	51,351
	69,252

The Company's objectives when managing capital are to safeguard its assets and maintain a globally competitive cost structure while looking for growth opportunities to provide returns to its shareholders. In addition, the Company works with relevant stakeholders to ensure the safety of its operations and employees, and remain in compliance with applicable environmental regulations and enhance the communities in which it operates.

The Company monitors and assesses on an ongoing basis its financial performance in order to ensure that its net debt levels are prudent taking into account the anticipated direction of the business cycle. The Company continuously monitors the public and private debt markets and the public equity markets in order to ensure that its capital structure is appropriately balanced. The Company can be influenced materially by changes in the relative value of the Canadian dollar, Swiss franc, United States dollar and euro.

The Company's capital comprises net debt and shareholders' equity as follows:

(thousands of dollars, unaudited)	September 30, 2017 \$	December 31, 2016 \$
Cash and cash equivalents	33,866	22,132
Less total debt	211,808	197,780
Net debt	(177,942)	(175,648)
Shareholders' equity	193,824	210,549

The Company has certain financial covenants stipulating subsidiary specific minimum ratios of working capital and debt to earnings, maximum ratios of long-term debt to adjusted net worth and debt service coverage, as well as certain non-financial covenants. Debt obligations are held by various entities within the Company with individual debt agreements specifying the entities within the Company that are to be included in the covenant calculations.

The Company ensures it remains in compliance with all of its existing debt covenants in order to facilitate future access to capital. Management reviews past results and forecasts to monitor their compliance. The Company was in compliance with all externally imposed capital requirements for the period ended September 30, 2017.

## **Outstanding Shares**

The number of common shares outstanding at September 30, 2017, and the date of this report was 14,238,552. The number of options outstanding at September 30, 2017 and the date of this report was 665,458 and 505,658 respectively. At September 30, 2017 and the date of this report there were 88,345 restricted share units outstanding. At September 30, 2017 and the date of this report there were 267,814 and 276,512 deferred share units outstanding, respectively.

## **Related Party Transactions**

Related party transactions consist of remuneration of directors and other key management personnel with whom we have entered into employment agreements. Further information is contained in our management information circulars in respect of our annual general meetings of shareholders, which are filed on SEDAR at [www.sedar.com](http://www.sedar.com).

## **Contingencies**

Provisions for liabilities relating to legal actions, tax reassessments and claims require judgment using management's best estimates regarding projected outcomes and the range of loss, based on such factors as historical experiences, stage of proceedings and recommendations of legal counsel and tax advisors. Actual results may vary from estimates and the differences are recorded when known.

In a judgement made in March 2017, all legal claims filed against the Company in the Supreme Court of British Columbia brought by Sateri (Shanghai) Management Limited and Sateri International (Singapore) Pte. Ltd. (together, "Sateri") were dismissed and in June 2017, a notice of abandonment of an appeal was filed by Sateri concluding the legal proceedings.

In July 2017, a product claim in the Security Paper Products Segment dating back to July 2012 was dismissed by the courts and a \$2.7 million reversal of a legal provision was recorded.

## **Critical Accounting Estimates**

For a review of significant management judgments affecting financial results and critical accounting estimates, see the Management's Discussion and Analysis for the year ended December 31, 2016 available on SEDAR.

## **New Accounting Pronouncements**

### **Accounting standards issued and not applied**

#### *IFRS 16 – Leases*

In January 2016, the IASB issued IFRS 16, Leases, which requires, among other things, lessees to recognize leases traditionally recorded as operating leases in the same manner as a financing lease. The required adoption date is January 1, 2019, with early adoption permitted. The Company is currently evaluating the impact from the adoption of this standard.

#### *IFRS 9 – Financial Instruments- Classification and Measurement*

The final version of IFRS 9 was issued in July 2014 and includes (i) a third measurement category for financial assets, and (ii) a single forward looking expected loss impairment model. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. The Company does not anticipate the new standard to have a significant impact on its financial statements.

### *Amendments to IFRS 7 - Financial Instruments: Disclosures*

IFRS 7 is amended to require additional disclosures on transition from IAS 39 to IFRS 9. The Amendment of IFRS 7 is effective on adoption of IFRS 9.

### *IFRS 15 - Revenue from Contracts with Customers*

This new standard on revenue recognition supersedes IAS 18 - Revenue, IAS 11 - Construction Contracts, and related interpretations. IFRS 15 is effective for the first interim period beginning on or after January 1, 2018. The Company is currently in the process of evaluating the impact of this standard on its financial statements and does not expect this standard to have a significant impact on the Company's consolidated financial statements. The Company expects to apply this standard on a modified retrospective basis using certain practical expedients. Under this approach, the 2017 comparative period will not be restated and a cumulative transitional adjustment to the opening balance of retained earnings will be recognized at the date of initial application.

### *IFRIC 23 - Uncertainty over Income Tax Treatments*

This interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 - Income Taxes when there is uncertainty over income tax treatments. This interpretation is effective for annual reporting periods beginning on or after January 1, 2019. The Company is currently evaluating the impact from the adoption of this interpretation.

There are no other standards or amendments or interpretations to existing standards issued but not yet effective which are expected to have a material impact on our consolidated financial statements.

### **Risks and Uncertainties**

A comprehensive discussion of risk factors is included in the Company's Annual Information Form dated March 31, 2017, available on SEDAR at [www.sedar.com](http://www.sedar.com). Those as well as risks detailed in the Management's Discussion and Analysis for the year ended December 31, 2016, also available on SEDAR, may impact the business of the Company.

### **Disclosure Controls and Internal Controls over Financial Reporting**

During the quarter ended September 30, 2017, there were no changes in the Company's internal controls over financial reporting that materially affected, or would be reasonably likely to materially affect, such controls.