CONIFEX

CONIFEX TIMBER INC.

2020 MANAGEMENT'S DISCUSSION AND ANALYSIS

March 2, 2021

*This Management's Discussion and Analysis ("**MD&A**") provides a review of the financial condition and results of operations of Conifex Timber Inc. ("**Conifex**", "**us**", "**we**", or "**our**"), on a consolidated basis, for the fiscal year ended December 31, 2020 relative to 2019. This MD&A should be read together with our audited consolidated financial statements for the year ended December 31, 2020 and notes thereon, which have been prepared in accordance with International Financial Reporting Standards ("**IFRS**") and filed on SEDAR at www.sedar.com.*

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

*In April 2019, we sold Lignum Forest Products LLP ("**Lignum**"), through which we operated a lumber marketing and distribution business, and in October 2019, we ceased operations at 0318587 B.C. Ltd. (previously Navcor Transportations Services Inc.) ("**031 BC**") through which we provided third party logistics services. In February 2020, we sold our US Sawmill Business (as defined herein). In accordance with IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, the operating results previously reported for Lignum, 031 BC and the US Sawmill Business were restated as discontinued operations for the relevant periods and separated from our continuing operations. Unless otherwise indicated, our discussion and analysis herein reflects our continuing operations. In accordance with IFRS 8, Operating Segments, we also combined our previous reporting segments, including our lumber and bioenergy operating segments, into a single reportable segment. Accordingly, all previously segmented information has been restated to conform to the current presentation for all periods presented. For further information, refer to Note 6 to our consolidated financial statements for the years ended December 31, 2020 and 2019.*

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

Forward-Looking Statements

This MD&A contains certain forward-looking information that reflects our current views and/or expectations with respect to our beliefs, assumptions, estimates and forecasts about our business and the industries and markets in which we operate. The reader is cautioned that statements comprising forward-looking information are not guarantees of future performance and involve known and unknown risks, uncertainties, assumptions and other factors which are difficult to predict and that may cause actual results or events to differ materially from those anticipated in such forward-looking information. Accordingly, readers should not place undue reliance on forward-looking information. Examples of such forward-looking information that *may be contained in this document include statements regarding: the realization of expected benefits of completed, current and any contemplated capital projects and the expected timing and budgets for such projects; the growth and future prospects of our business, including the impact of COVID-19 thereon; our expectations regarding our results of operations and performance; our planned operating format and expected operating rates; our perception of the industries or markets in which we operate and anticipated trends in such markets and in the countries in which we do business; our ability to supply our manufacturing operations with wood fibre and our expected cost for wood fibre; our expectation for market volatility associated with, among other things, the softwood lumber dispute with the U.S.; that we could be negatively impacted by the duties or other protective measures on our products, such as antidumping duties or countervailing duties on softwood lumber; continued positive relations with Aboriginal groups; the development of a longer-term capital plan and the expected benefits therefrom; demand and prices for our products; our ability to develop new revenue streams; the availability and use of credit facilities or proceeds therefrom; and future capital expenditures. Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking statements may include, but are not limited to, our future debt levels; that we will complete our projects in the expected timeframes and as budgeted; that we will effectively market our products; that capital expenditure levels will be consistent with those estimated by our management; our ability to obtain financing on acceptable terms, or at all; that interest and foreign exchange rates will not vary materially from current levels; the general health of the capital markets and the lumber industry and the general stability of the economic environments within the countries in which we operate or do business.*

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

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

RECENT DEVELOPMENTS

Normal Course Issuer Bid ("NCIB")

On November 26, 2020, the Toronto Stock Exchange (the "**TSX**") accepted our notice of intention to make a normal course issuer bid (the "**NCIB**") for our common shares. We commenced the bid because we believed the market price of our common shares did not reflect the value of our underlying business and future prospects. Therefore, we considered an allocation of capital to repurchase some of our common shares was an attractive option. Under the NCIB, we may purchase up to a maximum of 2,944,320 of our outstanding common shares. Pursuant to the NCIB, we may not repurchase more than (i) $5 million of our common shares between the period of November 30, 2020 and September 30, 2021 and (ii) $5 million of our common shares between the period of October 1, 2021 and the expiry of the bid. Any common shares acquired under the NCIB will be purchased at the market price up to a daily maximum of 12,500 common shares, being 25% of the average daily trading volume for the six months prior to the bid, subject to the block purchase exemption. All common shares acquired by us under the NCIB will be cancelled following purchase. The NCIB will terminate on November 30, 2021 or earlier if we have completed our purchases of the securities subject to the NCIB or if we otherwise determine that it is appropriate to suspend or terminate the bid. In December 2020, we purchased 584,400 shares under the NCIB.

Revolving Credit Facility

On October 13, 2020, we completed a $10.0 million secured revolving credit facility with Wells Fargo Capital Finance Corporation Canada (the "**Revolving Credit Facility**"). The Revolving Credit Facility is available for a term of 3 years and is substantially secured by our lumber inventory, equipment, and accounts receivable. The Revolving Credit Facility bears interest at CDOR or LIBOR plus a margin of 3.5% and contains an accordion feature to increase the limit of the Facility to $15.0 million, subject to certain conditions.

COVID-19 Pandemic

In response to the COVID-19 pandemic, we instituted certain measures to protect the health and safety of our employees in March 2020. This included adopting a pandemic contingency plan which includes restricting access to our offices and operation sites, restricting business travel for employees, mandating self-isolation for any staff exhibiting symptoms or having been exposed to the virus, practicing appropriate social distancing at our premises and increasing the frequency and emphasis on cleaning and sanitizing.

COVID-19's initial impact resulted in a deterioration of global demand for forest products. In response, in early April, we temporarily curtailed operations at our Mackenzie, British Columbia sawmill. The curtailment, which was initially scheduled for two weeks, was extended to July 6, 2020. As global demand for forest products improved and outpaced available supply, benchmark lumber prices increased significantly towards the end of the second quarter and reached record levels during the third quarter of 2020. We recommenced sawmill operations on July 6, 2020 and ramped-up to normalized operating rates during the third quarter of 2020.

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

Sale of US Sawmill Business

In February 2020, we sold our US sawmill business, consisting of our El Dorado, Cross City and Glenwood sawmills and related operations (the "**US Sawmill Business**") for US$172.8 million, including net working capital of US$9.8 million.

We utilized a majority of the proceeds from the sale to retire our previous secured credit facility that supported our lumber mills (the **"Retired Lumber Credit Facility**"). Our Conifex term loan supporting our electricity generation operations (the "**Power Term Loan**"), which is secured against our power assets and largely non-recourse to our lumber operations, represents substantially all of our remaining long-term debt.

SUMMARY OF 2020 RESULTS

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

Selected Financial Information(1)

(in millions of dollars, except as noted)	**2020**	**2019**	**2018**
Sales			
Lumber – Conifex produced	98.4	106.2	284.0
Lumber – wholesale	3.3	15.6	38.2
By-products	2.3	9.8	30.1
Bioenergy	24.7	25.8	26.8
	128.7	157.4	379.1
Operating income (loss)	3.4	(40.2)	19.8
Adjusted EBITDA(2) from continuing operations	13.8	(24.0)	32.4
Net income (loss) from continuing operations	(6.8)	(30.4)	(7.3)
Net income (loss) from discontinued operations	0.3	(169.8)	0.2
Net income (loss)	(6.5)	(200.2)	(7.1)
Basic and diluted earnings (loss) per share			
Continuing operations	(0.14)	(0.65)	(0.20)
Discontinued operations	-	(3.63)	0.01
Total basic and diluted earnings (loss) per share	(0.14)	(4.28)	(0.19)
Shares outstanding – weighted average (millions)	47.0	46.7	36.3

Selected Operating Information

Production – WSPF lumber (MMfbm)(3)	136.8	185.0	453.5
Shipments – WSPF lumber (MMfbm)(3)	134.4	211.9	458.2
Shipments – wholesale lumber (MMfbm)(3)	4.1	22.3	50.8
Electricity production (GWh)	202.5	211.0	211.3
Average exchange rate –$/US$(4)	0.745	0.754	0.772
Average WSPF 2x4 #2 & Btr lumber price (US$)(5)	$556	$360	$480
Average WSPF 2x4 #2 & Btr lumber price ($)(6)	$746	$478	$621

(1) Reflects results of continuing operations, except where otherwise noted.
(2) Conifex's adjusted EBITDA calculation represents earnings before finance costs, taxes, depreciation and amortization, foreign exchange translation gains or losses on long-term debt, restructuring costs, proceeds from insurance claims and gains or losses on sale of assets.
(3) MMfbm represents million board feet.
(4) Bank of Canada, www.bankofcanada.ca.
(5) Random Lengths Publications Inc.
(6) Average SPF 2x4 #2 & Btr lumber prices (US$) divided by average exchange rate.

REVIEW OF 2020 FINANCIAL RESULTS

Lumber Operations

Our lumber operating and financial results in 2020 were materially impacted by the curtailment of our Mackenzie sawmill from April 6 to July 6, 2020. In the second half of 2020, following the restart and gradual ramp-up to normalized operating levels, 86.2 million board feet of lumber was produced, reflecting an annualized operating rate of 72% of capacity. In 2019, our lumber operations include results from the Fort St. James sawmill which was curtailed in May 2019 and sold in November 2019. In 2019, 185.0 million board feet of lumber was produced from the Fort St. James and Mackenzie sawmills as a result of reduced daily operating configuration and the incurrence of intermittent curtailments during the year. Lumber production was 136.8 million board feet in 2020, representing a decrease of 26% in comparison to 2019 production.

Shipments of Conifex produced lumber totaled 134.4 million board feet in 2020. Shipments of lumber decreased by 37% from 2019 as a result of decreased production volumes, offset partially by a decrease in inventory from the prior year. Our wholesale lumber program shipped 4.1 million board feet in 2020.

Revenues from lumber products were $101.7 million in 2020 and represented a decrease of 16% from 2019. Lower revenues were driven by lower shipment volumes and wholesale activity, offset partially by significantly higher mill net realizations resulting from higher overall benchmark lumber prices in 2020.

Following the initial adverse economic impacts of the COVID-19 pandemic, North American lumber markets improved significantly during the second half of 2020. US housing starts on a seasonally adjusted annual basis recovered to levels reported prior to the COVID-19 pandemic. The increase in lumber demand, coupled with the impact of supply disruptions caused by the COVID-19 pandemic earlier in 2020, resulted in a significant increase to the benchmark Western SPF lumber price during the second half of 2020. Canadian dollar-denominated benchmark Western SPF prices increased by 56% from the prior year to $746 in 2020.

Cost of goods sold in 2020 were 40% lower than 2019 as a result of lower production and shipment volumes as unit operating costs were largely consistent year-over-year. We recorded a positive inventory valuation adjustment of $2.1 million in 2020 compared to $1.9 in 2019.

We expensed countervailing ("**CV**") and anti-dumping ("**AD**") duty deposits of $10.5 million in 2020, an increase of 18% from 2019. The duty deposits were based on a combined rate of 20.23% from January 1, 2020 to December 1, 2020, and 8.99% thereafter. These export taxes were significantly higher than 2019 on a unit basis due to the increased proportion of lumber shipments made to the stronger US market during 2020.

Bioenergy Operations

Our Mackenzie power plant sold 202.5 gigawatt hours of electricity under our Electricity Purchase Agreement ("**EPA**") with BC Hydro and Power Authority ("**BC Hydro**") in 2020, representing approximately 92% of targeted operating rates. In 2019, the Mackenzie power plant sold 211.0 gigawatt hours of electricity, representing 96% of targeted operating rates. The decrease in 2020 production was driven by a disruption in December 2020 caused by damage to the plant’s generator, resulting in 29 days of unplanned downtime. A replacement for the failed component of the power plant was procured from the original equipment manufacturer and installed in February. The power plant was successfully recommissioned and began producing electricity at normalized rates on February 21, 2021.

Our EPA with BC Hydro, similar to other electricity purchase agreements, provides BC Hydro with the option to "turn down" electricity purchased from us during periods of low demand by issuing a "dispatch order". BC Hydro issued a dispatch order for a period of 117 days, from April 24 to August 19, 2020. In 2019, our power plant was dispatched for 114 days, commencing in early May to August 31, 2019. We continue to be paid revenues under the EPA based upon a reduced rate and on volumes that are generally reflective of contracted amounts. During any dispatch period, we continue to produce electricity to fulfill volume commitments under our Load Displacement Agreement with BC Hydro (the "**LDA**").

Selling, General and Administrative Costs

Selling, general and administrative ("**SG&A**") costs of $6.5 million in 2020 reflected a decrease of 46% from 2019. We significantly reduced SG&A costs by reducing management personnel and overhead costs to better align our corporate support functions with our operating footprint. We incurred restructuring costs of $1.9 million in 2020 in relation to these cost reduction initiatives.

Finance costs and accretion

Finance costs and accretion of $7.2 million in 2020 were 83% lower than finance costs of $42.1 million in 2019 as a result of the repayment of the Retired Lumber Credit Facility on February 1, 2020. Finance costs incurred subsequent to February 1, 2020 relate primarily to the Power Term Loan.

Gain or Loss on Derivative Financial Instruments

Gains or losses on lumber derivative instruments are recognized as they are settled or as they are marked to market for each reporting period. Conifex does not presently use derivatives for trading or speculative purposes. In 2020, we entered into lumber futures contracts for downside price protection purposes on a small percentage of our estimated second-half 2020 production. Due to lumber market conditions characterized by rapidly rising prices from June to September 2020, we recorded a loss from lumber derivative instruments of $3.3 million in 2020. These futures contracts were closed and there were no outstanding futures contracts in place as at December 31, 2020.

Foreign Exchange Translation Gain or Loss

The foreign exchange translation gain or loss recorded for each period on our statement of net income results from the revaluation of US dollar-denominated cash, working capital balances and the Retired Lumber Credit Facility. US dollar-denominated monetary assets and liabilities are translated using the period end rate.

The foreign exchange translation impacts arising from the variability in exchange rates at each measurement period on our previous US dollar denominated Retired Lumber Credit Facility resulted in the recognition of a foreign exchange loss of $2.1 million in 2020 and a foreign exchange gain of $8.9 million in 2019. We recognized a foreign exchange gain of $1.9 million on cash and working capital balances in 2020, compared to a gain of $0.4 million in 2019.

Income tax

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities on our balance sheet and the amounts used for income tax purposes. We recorded a deferred income tax recovery of $0.4 million in 2020, and a deferred income tax recovery of $11.4 million in 2019.

Discontinued Operations

Net income from discontinued operations was approximately $0.3 in 2020 compared to a net loss from discontinued operations of $169.8 million 2019. The net loss in 2019 included an impairment loss allocated to goodwill of $143.1 million related to the sale of our US Sawmill Business. For further information on discontinued operations, see "Recent Developments – Sale of US Sawmill Business" above, and Note 6 to the consolidated financial statements for the years ended December 31, 2020 and 2019.

SUMMARY OF FOURTH QUARTER 2020 RESULTS

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

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

Selected Financial Information[(1)]

(unaudited, in millions of dollars, except as noted)	Q4 2020	Q3 2020	Q4 2019
Sales			
Lumber – Conifex produced	42.0	30.7	18.0
Lumber – wholesale	1.7	0.5	-
By-products	-	0.4	1.7
Bioenergy	6.1	6.0	8.0
	49.8	37.6	27.7
Operating income (loss)	4.6	7.0	(11.5)
Adjusted EBITDA[(2)] from continuing operations	6.8	7.6	(3.9)
Net income (loss) from continuing operations	2.2	2.0	(10.2)
Net income (loss) from discontinued operations	0.1	-	(152.4)
Net income (loss)	2.3	2.0	(162.6)
Basic and diluted earnings (loss) per share			
Continuing operations	0.05	0.04	(0.22)
Discontinued operations	-	-	(3.25)
Total basic and diluted earnings (loss) per share	0.05	0.04	(3.47)
Shares outstanding – weighted average (millions)	47.0	47.0	46.9
Selected Operating Information			
Production – WSPF lumber (MMfbm)[(3)]	48.3	48.0	37.8
Shipments – WSPF lumber (MMfbm)[(3)]	49.1	39.2	38.0
Shipments – wholesale lumber (MMfbm)[(3)]	1.8	0.7	-
Electricity production (GWh)	41.7	54.9	55.1
Average exchange rate –$/US$[(4)]	0.767	0.751	0.758
Average WSPF 2x4 #2 & Btr lumber price (US$)[(5)]	$700	$768	$380
Average WSPF 2x4 #2 & Btr lumber price ($)[(6)]	$912	$1,023	$502

(1) Reflects results of continuing operations, except where otherwise noted.
(2) Conifex's adjusted EBITDA calculation represents earnings before finance costs, taxes, depreciation and amortization, foreign exchange translation gains or losses on long-term debt, restructuring costs, proceeds from insurance claims and gains or losses on sale of assets.
(3) MMfbm represents million board feet.
(4) Bank of Canada, www.bankofcanada.ca.
(5) Random Lengths Publications Inc.
(6) Average SPF 2x4 #2 & Btr lumber prices (US$) divided by average exchange rate.

REVIEW OF FOURTH QUARTER 2020 FINANCIAL RESULTS

Lumber Operations

Our lumber operating results in the fourth quarter of 2020 were impacted by challenging logging conditions leading to a short period of downtime and resulting in operating rates of approximately 80% of annualized capacity. We produced 48.3 million board feet of lumber in the fourth quarter of 2020. In the previous quarter, 48.0 million board feet of lumber was produced following the restart and gradual ramp-up of operations. In the fourth quarter of 2019, we produced 37.8 million board feet of lumber as a result of the reduced daily operating configuration.

Shipments of Conifex produced lumber totaled 49.1 million board feet in the fourth quarter of 2020, representing an increase of 25% from the 39.2 million board feet of lumber shipped in the previous quarter and 29% from the 38.0 million board feet of lumber shipped in the fourth quarter of 2019 as a result of increased production volumes and a decrease in inventory from the previous quarter.

Revenues from lumber products were $43.7 million in the fourth quarter of 2020 and represented an increase of 40% from the previous quarter and an increase of 143% from the fourth quarter of 2019. Increased revenues were driven by higher shipment volumes and higher mill net realizations in the current quarter. Our lumber is typically sold 2-4 weeks in advance of its shipment date, resulting in a lag in our realized lumber prices when compared to concurrent reported lumber prices. As a result, a portion of the significant lumber price increase during the previous quarter was realized in the current quarter.

Following the significant increase in North American lumber market prices in the third quarter of 2020, activity and lumber prices adjusted downward in the fourth quarter but remained at historically elevated levels. US housing starts on a seasonally adjusted annual basis averaged 1,582,000 in the fourth quarter of 2020, up 10% from the previous quarter and 11% from the fourth quarter of 2019. Canadian dollar-denominated benchmark Western SPF prices, which averaged $912 in the fourth quarter of 2020, decreased by 11% or $111 from the previous quarter and increased by 82% or $410 from the fourth quarter of 2019.

Cost of goods sold in the fourth quarter of 2020 increased by 60% from the previous quarter and 13% from the fourth quarter of 2019 as a result of higher overall shipments in the current quarter. Unit costs increased in comparison to the previous quarter and were significantly below the fourth quarter of 2019 as a result of a reduced operating format in the prior year.

We expensed CV and AD duty deposits of $4.6 million in the fourth quarter of 2020, $3.7 million in the previous quarter and $1.4 million in the fourth quarter of 2019. The duty deposits were based on a combined rate of 20.23% until December 1, 2020 and 8.99% thereafter.

Bioenergy Operations

Our Mackenzie power plant sold 41.7 gigawatt hours of electricity under our EPA with BC Hydro in the fourth quarter of 2020, representing approximately 75% of targeted operating rates. The Mackenzie power plant sold 54.9 and 55.1 gigawatt hours of electricity in the previous quarter and fourth quarter of 2019, respectively. The relative decrease in production in the fourth quarter of 2020 resulted from the disruption in December 2020 caused by damage to the plant’s generator, causing 29 days of unplanned downtime. A replacement for the failed component of the power plant was procured from the original equipment manufacturer and installed in February. The power plant was successfully recommissioned and began producing electricity at normalized rates on February 21, 2021.

Selling, General and Administrative Costs

SG&A costs of $1.1 million in the fourth quarter of 2020 reflected a decrease of 40% from the fourth quarter of last year, driven by reduced management personnel and overhead costs.

Finance costs and accretion

Finance costs and accretion totaled $1.3 million in the fourth quarter of 2020, $1.2 million in the previous quarter and $21.7 million in the fourth quarter of 2019. Finance costs in the fourth quarter of 2019 related primarily to the Retired Lumber Credit Facility and included $13.0 million for the recognition of unamortized financing fees in the quarter. Finance and interest costs subsequent to February 1, 2020 relate primarily to the Power Term Loan.

SUMMARY OF FINANCIAL POSITION

(in millions of dollars, unless otherwise noted)	2020	2019	2018
Cash	11.2	0.9	16.3
Cash – restricted	3.6	6.7	8.6
Operating working capital(1)	14.7	2.8	86.1
Current portion of revolver and long-term debt	(4.5)	(194.0)	(46.4)
Assets held for sale	-	236.5	0.9
Liabilities held for sale	-	(21.5)	-
Net current assets	25.0	31.4	65.5
Property, plant and equipment	130.0	137.3	382.1
Other long-term assets	37.9	38.0	194.7
	192.9	206.7	646.5
Non-interesting bearing long-term liabilities	17.6	18.8	20.8
Long-term debt – Power Term Loan	57.0	60.2	63.4
Long-term debt – other(2)	1.9	3.1	221.2
Shareholders' equity	116.4	124.6	340.1
	192.9	206.7	646.5
Ratio of current assets to current liabilities	2.0	1.1	0.5
Net debt to capitalization	29%	67%	48%
Net debt (cash) to capitalization excluding Power Term Loan	(3%)	61%	42%

(1) Calculated as the aggregate of trade and other receivables, prepaid expenses and deposits and inventories less the aggregate of trade payables, accrued liabilities and other payables, the current portion of reforestation obligations and employee liabilities.
(2) Consists of leases in 2020 and 2019.

Operating working capital increased by $11.9 million in 2020 due primarily to a reduction in trade payables of $20.9 million, offset partially by a reduction in inventory and prepaid expenses and deposits. Inventory levels were lower than the prior year due to lower log inventory held at December 31, 2020.

Overall debt was $63.4 million at December 31, 2020 compared to $257.2 million at December 31, 2019. The reduction of $193.8 million in debt comprised repayment in full of our Retired Lumber Credit Facility of $189.4 million, lease repayments of $1.4 million and Power Term Loan payments of $3.0 million. Our Power Term Loan, which is largely non-recourse to our lumber operations, represents substantially all of our outstanding long-term debt. At December 31, 2020, we had $60.3 million outstanding on our Power Term Loan, while our remaining long-term debt, consisting of leases, was $3.1 million.

As at December 31, 2020, $103.1 million of our consolidated property, plant and equipment was attributable to our power operations.

The ratio of current assets to current liabilities was 2.0:1 at December 31, 2020 compared to 1.1:1 at December 31, 2019. This change was attributable to an increase in cash on hand, reduced accounts payable and due to the sale of the US Sawmill Business and the full repayment of the Retired Lumber Credit Facility which was classified as a current liability as at December 31, 2019.

We use the net debt to total capitalization ratio to measure our relative debt position and as an indicator of the relative strength and flexibility of our balance sheet. Net debt is calculated as interest-bearing debt less cash. Total capitalization is calculated as the sum of net debt and equity. Net debt at December 31, 2020 decreased by $201.0 million to $48.6 million from $249.6 million at December 31, 2019. The net debt to capitalization ratio was approximately 29% at December 31, 2020 and 67% at December 31, 2019.

LIQUIDITY AND CAPITAL RESOURCES

Summary of Cash Flows

(millions of dollars)	2020	2019
Cash generated from (used in)		
Operating activities	10.4	(9.1)
Change in non-cash working capital	(16.7)	52.0
Investing activities	221.5	47.2
Financing activities and other	(207.4)	(107.2)
Increase (decrease) in cash	7.8	(17.1)

Operating Activities

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

Operating activities before changes in non-cash working capital generated $10.4 million of cash in 2020, compared to net cash usage of $9.1 million in 2019. Changes in non-cash working capital used $16.7 million of cash in 2020 and generated $52.0 million in 2019. We generated significant cash from working capital in 2019 with reduced operations and the release of working capital balances following the curtailment of the Fort St. James sawmill.

Investing Activities

Investing activities generated cash of $221.5 million in 2020, comprised primarily of $223.6 million from the sale of our US Sawmill Business. Investing activities in 2019 generated $47.2 million, including net proceeds of $14.7 million from the sale of Lignum and $38.7 million from the sale of the Fort St. James sawmill.

Financing Activities

Our financing activities used net cash of $207.4 million in 2020 including $191.8 million to repay in full the Retired Lumber Credit Facility, finance expenses of $9.6 million and purchases of $0.9 million of Conifex shares under the NCIB. In 2019, financing activities used net cash of $107.2 million, comprised primarily of repayments of borrowings of $70.0 million and the payment of finance expenses of $25.0 million.

Liquidity

Our principal sources of funds are cash on hand, cash flow from operations and cash available under the $10.0 million Revolving Credit Facility. Our principal uses of funds consist of operating expenditures, capital expenditures, interest payments and repayment of principal on our Power Term Loan.

On October 13, 2020, we completed a $10.0 million secured revolving credit facility with Wells Fargo Capital Finance Corporation Canada. The Revolving Credit Facility is available for a term of 3 years and is substantially secured by Conifex's lumber inventory, equipment and accounts receivable.

At December 31, 2020, we had total liquidity of $21.2 million, compared to $5.2 million at December 31, 2019. Liquidity at December 31, 2020 was comprised of unrestricted cash of $11.2 million and unused availability of $10.0 million under the Revolving Credit Facility.

The increase in our liquidity in 2020 was primarily from the net proceeds received from the sale of our US Sawmill Business in the first quarter of 2020, partially offset by the repayment in full of our Retired Lumber Credit Facility, an increased investment in non-cash working capital and the addition of the Revolving Credit Facility which was undrawn as at December 31, 2020.

Like other Canadian lumber producers, we were required to begin depositing cash on account of softwood lumber duties imposed by the United States government in April 2017. Cumulative duties of US$10.2 million paid by the Company, net of sales of the right to refunds, since the inception of the current trade dispute remain held in trust by the US pending the administrative reviews and conclusion of all appeals of US decisions. We expect future cash flow will continue to be adversely impacted by the CV and AD duty deposits to the extent additional costs on US destined shipments are not mitigated by higher lumber prices.

We monitor our expected liquidity levels and compliance with debt covenants under our Power Term Loan and Revolving Credit Facility by regularly preparing rolling cash flow forecasts to consider upcoming operational requirements, debt service commitments and future business development. We did not have any material commitments for capital expenditures at December 31, 2020. Based on our current level of operations and our present expectations for future periods in light of the existing economic environment, we believe that cash flow from operations, flexibility in levels of investment in operating working capital and availability under the Revolving Credit Facility will be adequate to meet our obligations over the next twelve months.

Contractual Obligations

The following table summarizes the estimated aggregate amount of future cash outflows for contractual obligations with exclusions as noted below:

	Payments due by Period				
	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Long term debt	90.8	7.0	14.0	14.0	55.7
Leases	3.1	1.3	1.5	0.3	-
Reforestation obligations	11.8	3.6	3.3	1.1	3.8
Trade payables and accrued liabilities	14.8	14.8	-	-	-
Provisions and other liabilities	12.1	1.2	9.8	0.2	1.0
	132.6	27.9	28.6	15.6	60.5

Off-Balance Sheet Arrangements

Our off-balance sheet arrangements as at December 31, 2020 were comprised of standby letters of credit totalling $5.6 million posted by our subsidiary Conifex Power Limited Partnership. The standby letters of credit are issued to BC Hydro in connection with the EPA and the LDA.

Transactions Between Related Parties

Other than transactions in the normal course of business with key management personnel, we had no transactions between related parties in 2020.

SELECTED QUARTERLY FINANCIAL INFORMATION

Quarterly Earnings Summary

(in millions of dollars, unless otherwise noted)	2020 Q4	2020 Q3	2020 Q2	2020 Q1	2019 Q4	2019 Q3	2019 Q2	2019 Q1
Sales	49.8	37.6	10.8	30.6	27.7	22.9	40.1	66.8
Operating income (loss)	4.6	7.0	(1.4)	(6.8)	(11.5)	(8.6)	(11.7)	(8.5)
Net income (loss) from continuing operations	2.2	2.0	(2.7)	(8.2)	(10.2)	(11.6)	(1.1)	(7.4)
Net income (loss) – total operations	2.3	2.0	(3.0)	(7.7)	(162.6)	(16.6)	(9.1)	(11.9)
Net income (loss) per share – basic and diluted from continuing operations	0.05	0.04	(0.05)	(0.18)	(0.22)	(0.25)	(0.02)	(0.16)
Net income (loss) per share – basic and diluted – total operations	0.05	0.04	(0.06)	(0.17)	(3.47)	(0.35)	(0.19)	(0.25)
Adjusted EBITDA from continuing operations[1]	6.8	7.6	(1.1)	0.5	(3.9)	(7.0)	(9.1)	(4.0)
Shares outstanding – weighted average (in millions)	47.0	47.0	46.9	46.9	46.9	46.9	46.6	46.6
Statistics (in millions, except rate and prices)								
Production – WSPF lumber	48.3	48.0	2.4	38.2	37.8	26.0	47.6	73.5
Shipments – WSPF lumber	49.1	39.2	8.5	37.6	38.0	34.8	60.4	78.7
Shipments – wholesale lumber	1.8	0.7	1.6	-	-	0.3	5.4	16.6
Electricity production – GWh	41.7	54.9	51.2	54.8	55.1	53.1	47.2	55.6
Average exchange rate – $/US$[2]	0.767	0.751	0.722	0.744	0.758	0.757	0.748	0.752
Average WSPF 2x4 #2 & Btr lumber price (US$)[3]	700	768	357	399	380	356	333	372
Average WSPF 2x4 #2 & Btr lumber price ($)[4]	912	1,023	494	536	502	470	445	495
Reconciliation of Adjusted EBITDA to net income (loss)								
Net income (loss) from continuing operations	2.2	2.0	(2.7)	(8.2)	(10.2)	(11.6)	(1.1)	(7.4)
Add: Finance costs	1.3	1.2	1.2	3.5	21.7	7.0	7.4	6.0
Amortization	2.8	2.9	1.1	2.9	4.8	1.8	2.5	4.1
Deferred income tax expense (recovery)	0.5	1.5	(0.8)	(1.7)	(3.8)	(4.0)	(0.9)	(2.1)
EBITDA[5]	6.8	7.6	(1.2)	(3.5)	12.5	(6.8)	7.9	0.6
Add: Foreign exchange (gain) loss on long-term debt	-	-	-	2.1	(2.4)	2.4	(4.4)	(4.5)
Restructuring costs	-	-	0.1	1.9	2.6	-	-	-
Proceeds from insurance claim	-	-	-	-	(1.1)	-	-	-
Gain on sale of assets	-	-	-	-	(15.5)	-	-	(0.1)
Gain on sale of right to duty refunds	-	-	-	-	-	(2.6)	(12.6)	-
Adjusted EBITDA from continuing operations	6.8	7.6	(1.1)	0.5	(3.9)	(7.0)	(9.1)	(4.0)

(1) Conifex's adjusted EBITDA calculation represents earnings before finance costs, taxes, depreciation and amortization, foreign exchange translation gains or losses on long-term debt, restructuring costs, proceeds from insurance claims and gains or losses on sale of assets.
(2) Bank of Canada, www.bankofcanada.ca.
(3) Random Lengths Publications Inc. (Western Spruce/Pine/Fir, per thousand board feet).
(4) Average WSPF 2x4 #2 & Btr lumber prices (US$) divided by average exchange rate.
(5) Conifex's EBITDA calculation represents earnings before finance costs, taxes, and depreciation and amortization.

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

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

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

OUTLOOK

We expect lumber markets to remain strong in 2021, supported by robust demand from US housing starts and continued strength in the repair and remodeling sector. At the Mackenzie sawmill, we expect to achieve annualized operating rates of approximately 90% in 2021. Following the successful resumption of Mackenzie power plant operations in February 2021, we plan to operate at full capacity, subject to the optional “turn down” notice that may be received from BC Hydro during seasonal low demand periods.

As our liquidity and financial position are forecasted to continue to strengthen in the first half of 2021, funding quick payback sawmill upgrades and our share repurchase program remain key priorities.

Reconciliation of annual Adjusted EBITDA to net income (loss)

	2020	**2019**	**2018**
Net income (loss) from continuing operations	(6.8)	(30.4)	(7.3)
Add: Finance costs	7.2	42.1	16.6
Amortization	9.7	13.2	15.6
Income tax expense (recovery)	(0.4)	(10.8)	(1.3)
EBITDA[(1)]	9.7	14.1	23.6
Add: Foreign exchange (gain) loss on long-term debt	2.1	(8.9)	8.8
Restructuring costs	2.0	2.6	-
Proceeds from insurance claim	-	(1.1)	-
Gain on sale of assets	-	(15.5)	-
Gain on sale of right to duty refunds	-	(15.2)	-
Adjusted EBITDA from continuing operations	13.8	(24.0)	32.4

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

CRITICAL ACCOUNTING ESTIMATES

The preparation of the consolidated financial statements in conformity with IFRS requires management to make critical judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could materially differ from those estimates. Such difference in estimates are recognized when realized on a prospective basis.

The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are described below.

Valuation of Inventory

We closely monitor conditions that could impact valuation of inventories or otherwise impair our assets. Inventories of logs and lumber products are valued at the lower of average cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs for completion and applicable variable selling expenses. Our estimated selling price is based on our order file that exists at balance sheet reporting dates and management’s estimate for forecasted sales prices based on supply, demand and industry trends. Prices fluctuate over time and it is probable that market values at the time of eventual sale will differ from our estimates.

Write-downs of inventory cost to net realizable value, if any, are included in cost of goods sold when incurred and reported in the lumber segment operating results. Inventory was not written down as at December 31, 2020 (2019 - $2.1 million)

Valuation of Long-Lived Assets

Assets that have an indefinite useful life, such as goodwill, are not subject to amortization and are tested for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Impairment losses are recognized in net income for the period for the amount by which the asset's carrying amount exceeds its recoverable amount. An impairment analysis requires the use of significant assumptions, including management and independent third party input.

We review the amortization periods for our manufacturing equipment and machinery to ensure that the periods appropriately reflect anticipated obsolescence and technological change. Current amortization periods for manufacturing equipment range from 5 to 50 years. Timber licences are amortized over 60 years.

Management currently believes that Conifex has adequate support for the carrying value of its long-lived assets based on analysis including anticipated cash flows that result from our estimates of future demand, pricing and production costs, and assuming certain levels of planned capital expenditures. However, should the markets for Conifex's products deteriorate to levels significantly below current forecasts or should capital not be available to fund operations or expenditures, it is possible that we will be required to record further impairment charges.

Net impairment losses and recoveries are reported as a separate line item on the financial statements as non-operating items. The Company did not record any impairment losses or recoveries in 2020. The Company recorded an impairment loss, allocated to goodwill, of $143.1 million in net loss from discontinued operations in 2019 due primarily to the divestment of the US Sawmill Business.

Reforestation Obligation

Timber is harvested under various licences issued by the Province of British Columbia, which include future requirements for reforestation. The future estimated reforestation obligation is accrued based upon the volume of timber cut each period and charged to costs of goods sold in the lumber segment. The estimates of reforestation obligations are based upon various judgments and assumptions. Both the precision and reliability of such estimates are subject to uncertainties and, as additional information becomes known, these estimates are subject to change. The Company accrued $2.1 million in 2020 (2019 - $3.9 million) for future estimated reforestation obligations.

Environmental Remediation Costs

Costs associated with environmental remediation obligations are accrued and expensed when there exists a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Such accruals are adjusted as further information develops or circumstances change. Estimated costs of future expenditures for environmental remediation obligations are discounted to their present value when the amount and timing of expected cash payments are reliably determinable. Accruals for estimated environmental remediation obligations are charged to cost of goods sold in the lumber segment. There were no accruals made in 2020 or 2019.

Deferred Income Taxes

Deferred tax assets and liabilities comprise the tax effect of temporary differences between the carrying amount and tax basis of assets and liabilities, as well as the tax effect of unused tax losses. Assumptions underlying the composition of deferred tax assets and liabilities include estimates of future results of operations and the timing of reversal of temporary differences as well as the substantively enacted tax rates and laws at the time of the expected reversal. The composition of deferred tax assets and liabilities is reasonably likely to change from period to period due to the number of variables associated with the differing tax laws and regulations across the jurisdictions in which the Company operates. As a result, the precision and reliability of the resulting estimates are subject to uncertainties and may change as additional information becomes known. Uncertainties surrounding these assumptions and changes in tax rates or tax policy could have a material effect on expected results. The Company only recognizes a deferred income tax asset to the extent that the future realization of the tax asset is probable. This is based on our estimates and assumptions as to the future financial performance of the various taxable legal entities.

As at December 31, 2020, the Company recognized deferred income tax assets of $9.9 million and deferred income tax recovery of $0.4 million from continuing operations. As at December 31, 2019, the Company recognized deferred income tax assets of $9.5 million and recorded deferred income tax recovery of $11.4 million from continuing operations.

At December 31, 2020, the Company had unused non-capital tax losses carried forward totalling $208.6 million (December 31, 2019: $121.8 million). The Company has not recognized deferred income tax assets related to discontinued operations due to the uncertainty of future realization.

RISKS AND UNCERTAINTIES

The Company is exposed to many risks and uncertainties in conducting its business, including, but not limited to those factors described below.

Fluctuations in Prices and Demand for and Selling Price of Lumber

Our financial performance principally depends on the demand for and selling price of lumber, which is subject to significant fluctuations. The markets for lumber are highly volatile and are affected by many factors such as North American economic conditions, including the strength of the U.S. housing market, the Asian market, changes in industry production capacity, changes in inventory levels and other factors beyond our control. In addition, unemployment levels, interest rates, the availability of mortgage credit and the rate of mortgage foreclosures have a significant effect on residential construction and renovation activity, which in turn influence the demand for and price of lumber. A decline in demand and a corresponding reduction in prices for our products may adversely affect our financial condition and results of operations.

Liquidity Risk

Liquidity risk is the risk that a company will be unable to meet its financial obligations on a current basis. We manage liquidity risk through regular cash-flow forecasting and undertaking appropriate financing activities as required. We intend to finance our planned capital expenditures and scheduled debt payments from existing cash reserves and cash flow from operations.

Although we believe our actions will result in sufficient liquidity, there can be no assurance that we will be successful or that market conditions or competition will not work to offset our actions. The availability of funding, or other sources of capital, is dependent on capital markets at the relevant time and may not be available on acceptable terms or at all. In the event that debt or equity capital is not available on acceptable terms, or at all, in the future, we may need to explore other strategic alternatives. In addition, our credit facilities require us to satisfy certain financial covenants. There can be no assurance that we will be able to meet such covenants. A failure to meet such covenants could also result in our lenders accelerating some or all of our then outstanding indebtedness under our loans, which would have a material adverse effect on our business, financial condition and operating results. A failure to meet our financial covenants could also result in our lenders seeking to enforce their security against our power assets, which would materially adversely affect our business, financial condition and operating results.

Fibre Availability and Cost

The Mackenzie mill's log requirements are met using logs harvested from our timber tenures, by long-term trade and purchase agreements and by purchases on the open market and through timber sale bids. Currently, the timberlands in which we operate are owned by the Province of British Columbia and administered by the Ministry of Forests. The Forest Act, RSBC 1996, c 157 (the "Forest Act") empowers the Ministry of Forests to grant timber tenures to producers. The Provincial Chief Forester conducts a review of the AAC for each TSA on a periodic basis, which generally occurs once every five to ten years. This review then provides the basis upon which the AAC for licences issued by the Province of British Columbia under the Forest Act are determined. There are many factors that affect AAC, such as timber inventory, the amount of operable forest land, growth estimates of young forests, regulation changes and environmental and social changes.

We rely on third party independent contractors to harvest timber in areas over which we hold timber tenures. Increases in rates charged by these independent contractors or the limited availability of these independent contractors may increase our timber harvesting costs. Additionally, in order to ensure uninterrupted access to logs harvested from our timber tenures, we must focus on the continuous development of road networks and, in the Mackenzie operating area, the maintenance of remote logging camps and vessels and equipment related to delivery of logs by waterways. In addition, our ability to harvest fibre for use in our operations could be adversely impacted by natural events such as forest fires, severe weather conditions or insect infestations.

Fluctuations in the price, quality or availability of log supply could have a material effect on our business, financial position, results of operations and cash flow.

Public Health Crises, including COVID-19

Our business, operations and financial condition could be materially adversely affected by the outbreak of epidemics, pandemics or other health crises, such as the outbreak of the novel coronavirus that was designated as a pandemic by the World Health Organization on March 11, 2020. The international response to the spread of COVID-19 has led to significant restrictions on travel, temporary business closures, quarantines, global stock market volatility and a general reduction in consumer activity. Such public health crises can result in operating and supply chain delays and disruptions, global stock market and financial market volatility, declining trade and market sentiment, reduced movement of people and labour shortages, and travel and shipping disruption and shutdowns, including as a result of government regulation and prevention measures, or a fear of any of the foregoing, all of which could affect commodity prices, interest rates, credit ratings, credit risk and inflation.

Following initial disruptions to the global demand for global forest products, and resultant curtailment to our operations, Covid-19 has not had an adverse impact on our operations , which follows improved benchmark lumber prices for lumber as global demand for first products outpaced supply. However, we may experience business interruption, including suspended or reduced operations at our Mackenzie mill and power plant, expenses and delays, relating to COVID-19 as the pandemic continues to evolve and other such events outside of our control, which could have a material adverse impact on our business, operating results, financial condition and the market for our securities. It is unknown whether and how we may be affected if the pandemic continues to persist for any extended period of time, including the detection of new strands or variants of the virus. Our exposure to such public health crises also includes risks to employee health and safety. For information on our response to the COVID-19, see "Recent Developments – Covid-19 Pandemic" above.

Currency Risk

Our Mackenzie mill sells a significant majority of its lumber at prices denominated in U.S. dollars or based on prevailing U.S. dollar prices, but nearly all of our operating costs and expenses are incurred in Canadian dollars. Therefore, an increase in the value of the Canadian dollar relative to the U.S. dollar reduces the revenue in Canadian dollar terms realized by our Mackenzie mill from sales in U.S. dollars, which reduces operating margin and cash flow available to fund operations. We are also exposed to the risk of exchange rate fluctuations in the period between sale and payment, which results in significant earnings sensitivity to changes in the Canadian/U.S. dollar exchange rate.

We do not currently hedge our foreign exchange exposure with financial forward or open contracts, as the Canadian/U.S. dollar exchange rate is affected by a broad range of factors, making future rates difficult to predict.

Competition

Markets for our lumber are highly competitive. Our ability to maintain or improve the cost of producing and delivering products to those markets is crucial. Factors such as cost and availability of raw materials, energy, labour, the ability to maintain high operating rates and low per-unit manufacturing costs and the quality of our final products and customer service all affect earnings. Additionally, our products are sold in markets where we compete against many producers, many of whom have larger capacity than us, including when measured by the number of mills owned and operated. Many of our competitors have existed for a longer period of time and have significantly greater financial resources than us.

Commodity products have few distinguishing properties from producer to producer, therefore competition for these products is based primarily on price, which is determined by supply, relative to demand and competition from substitute products. The prices we receive for our products are affected by many factors that are outside of our control and we have little to no influence over the timing and extent of price changes, which can be volatile. Accordingly, our revenues and results from operations may be negatively affected by pricing decisions made by our competitors and by the decision of our customers to purchase products from our competitors.

Softwood Lumber Trade Dispute

Canadian softwood lumber exports to the U.S. have been the subject of trade disputes and managed trade arrangements for the last several decades. After the expiry of the last trade agreement between Canada and the U.S. in 2015, a group of U.S. lumber producers and timberland owners petitioned the U.S. Department of Commerce (the "**USDOC**") and the U.S International Trade Commission (the "**USITC**") to impose trade sanctions against Canadian softwood lumber exports to the U.S. The USDOC announced its preliminary determination on CV Duty ("**CVD**") and AD Duty ("**ADD**") rates in April and June 2017, respectively. On December 28, 2017, the USITC published its notice of final affirmative determination of material injury, which brought into effect the final amended "all other" CVD rate of 14.19% and ADD rate of 6.04%, for a combined rate of 20.23%.

The U.S. duty rate determinations are subject to annual Administrative Reviews, and revised combined CVD and ADD rates for the years ended December 31, 2017 and December 31, 2018 of 8.83% and 8.99%, respectively, were announced in the fourth quarter of 2020. The combined CVD and ADD rate of 8.99% applies for all lumber shipments from December 1, 2020 onwards, subject to the annual Administrative Reviews of the USDOC. The duties are likely to remain in place until and unless some form of trade agreement can be reached between Canada and the U.S. or a final binding determination is made as a result of litigation. Unless the additional costs imposed by duties can be passed to lumber consumers, the duties will increase costs for Canadian producers and, in certain cases, could result in some Canadian production becoming unprofitable. Whether and to what extent duties can be passed along to consumers will largely depend on the strength of demand for softwood lumber, which is influenced by a number of factors.

Like other Canadian forest product companies and the Canadian federal and provincial governments, we deny the U.S. allegations and disagree with the final determinations made by the USDOC and USITC, and collectively continue to aggressively defend the Canadian industry in this trade dispute. The federal government is appealing the US findings and will defend itself against claims of unfair trade practices made by the U.S. As in previous trade cases, the softwood lumber dispute may take years to resolve through the legal process and remains open to a negotiated settlement at any time.

The emergence of significant demand from China and other export markets in recent years has somewhat reduced our dependence on the U.S. market and the impact of potential cross-border trade disputes. Revenues generated from electricity sales are expected to provide further sources of cash flow diversification to mitigate the adverse effects of trade sanctions on softwood lumber by the U.S.

Cumulative duties of US$43.0 million paid by Conifex since inception of the current trade dispute remain held in trust by the US pending the First Administrative Review and conclusion of all appeals of US decisions. We have recorded the duty deposits as an expense. In 2019, we sold our right to refunds of cumulative duties of US$32.7 million for proceeds of US$13.9 million.

Capital Projects

We undertake ongoing maintenance activities and capital improvement projects at our facilities. Capital projects require significant commitment of our financial and other resources, and the results of a project may not be immediately known or assessable. We conduct cost-benefit and other analyses prior to the commencement of each capital project to measure the feasibility and expected benefits of proposed projects against pre-established criteria. Each material capital project is approved by our Board. We assign experienced project managers to each project and commit other resources as required, and, to date, have employed demonstrated technology. We are subject to numerous risks related to the undertaking of capital projects, including extensive reliance on third party equipment manufacturers and installers, material cost and time overruns, equipment or technology failure, major unplanned disruptions to existing operations and the failure of a completed project to deliver expected benefits. The realization of any of these risks could have a material adverse effect on our business, financial condition and operating results.

Wood Dust Management

The wood products industry and government regulators continue to make the management of combustible wood dust within sawmill manufacturing facilities a high priority. Conifex continues to take steps to mitigate the risks of combustible dust incident at our Mackenzie mill, including significant capital investment, a formalized wood dust control program, and employee training. Regulatory agencies have implemented various regulatory and inspection initiatives related to wood dust management. Additional regulatory initiatives including stop work conditions within the industry have occurred, and continue to be a possibility.

Transportation Limitations

We rely primarily on third parties for transportation of our products, as well as delivery of raw materials, a significant portion of which are transported by railroads, trucks and ships. If any of our third party transportation providers fails to deliver the raw materials or products or to distribute them in a timely manner, we may be unable to sell those products at full value, or at all, or may be unable to manufacture our products in response to customer demand, which could have a material adverse effect on our financial condition and results of operations. In addition, if any of these third parties ceases operations, suffers labour-related or other disruptions (including blockades), or ceases doing business with us, our operations or cost structure may be adversely impacted. From time to time, we may also face shortages of rail cars, trucks, containers, ships or other transportation methods that may limit raw material deliveries to us and product deliveries by us to our customers, which may have a material adverse effect on our business.

Operational Curtailments

From time to time, we may suspend or curtail operations at our Mackenzie mill, Mackenzie power plant, or one or more of our logging operations in response to market conditions, environmental risks, workplace safety concerns or other operational issues, including power failure, equipment breakdown, dry forest conditions, adverse weather conditions, labour disruptions, fire hazards or public health restrictions. These unscheduled operational suspensions or curtailments could have a material adverse effect on our financial condition and results of operations. Furthermore, pulp and paper mill production curtailments may require sawmills to find other ways to dispose of residual wood fibre and may result in curtailment or suspension of lumber production.

Regulatory Risks

Our operations are subject to extensive general and industry-specific federal, provincial, municipal and other local laws and regulations, including those governing forestry, exports, taxes, employees, labour standards, occupational health and safety, waste disposal, environmental protection and remediation, protection of endangered and protected species and land use and expropriation. We are required to obtain approvals, permits and licences for our operations, which may impose conditions that must be complied with. If we are unable to extend or renew, or are delayed in extending or renewing, a material approval permit or licence, our operations or financial condition could be adversely affected. There is no assurance that these laws, regulations or government policy, or the administrative interpretation or enforcement of existing laws, regulations and government policies, will not change in the future in a manner that may require us to incur significant capital expenditures or could adversely affect our operations or financial condition. Failure to comply with applicable laws or regulations, including approvals, permits and licences and new laws and regulations, could result in fines, penalties or enforcement actions, including orders suspending or curtailing our operations or requiring corrective measures or remedial actions.

Reliance on Directors, Management and Other Key Personnel

Our success depends in part on our ability to attract and retain senior management and other key employees. Competition for qualified personnel depends on, among other things, economic and industry conditions, competitors' hiring practices and the effectiveness of our compensation programs. The loss of, or inability to recruit and retain, any such personnel could impact our ability to execute on our strategies.

Information Systems Security Threats

We use information technologies ("IT") to assist in managing our operations and various business functions. We rely on various IT to process, store and report on our business and to communicate electronically between our facilities, personnel, customers and suppliers. We also use IT to process financial information and results of operations for internal reporting purposes and to comply with regulatory, legal and tax requirements. We have entered into agreements with third parties for hardware, software, telecommunications and other IT services in connection with our operations. Our operations depend, in part, on how well we and our IT suppliers protect networks, equipment, IT systems and software against damage from a number of threats, including, but not limited to, cable cuts, damage to physical plants, natural disasters, terrorism, fire, power loss, telecommunications failure, hacking, computer viruses, vandalism and theft and other security issues. Our IT systems may also be breached due to employee error, malfeasance or other disruptions. Our operations also depend on the timely maintenance, upgrade and replacement of networks, equipment, IT systems and software, as well as pre-emptive expenses to mitigate the risks of failures. Any of these and other events could result in information system failures, misappropriation of sensitive data, delays and/or increases in capital expenses. The failure of information systems or a component of information systems could, depending on the nature of any such failure, adversely impact our reputation, business, financial condition and results of operations or subject us to civil or criminal sanctions.

Although we have not to date experienced any material losses relating to cyber-attacks or other information security breaches, there can be no assurance that we will not incur such losses in the future. Our risk and exposure to these matters cannot be fully mitigated because of, among other things, the evolving nature of these threats. As a result, cyber security and the continued development and enhancement of controls, processes and practices designed to protect systems, computers, software, data and networks from attack, damage or unauthorized access remain a priority. As cyber threats continue to evolve, we may be required to expend additional resources to continue to modify or enhance protective measures or to investigate and remediate any security vulnerabilities.

Natural and Human-Made Disasters and Climate Change

Our operations are subject to adverse natural events such as forest fires, severe weather conditions, climate change, timber disease and insect infestation and earthquake activity. These events could damage or destroy our physical facilities or our timber supply, and similar events could also affect the facilities of our suppliers or customers. Any such damage or destruction could adversely affect our financial results.

Changing weather patterns and climate conditions due to natural and human-made causes have added to the unpredictability of the risks to our timber tenures and other standing forests, in particular forest fires, wind storms, insect infestations and disease. Procedures and controls are in place to manage such risk through prevention and early detection. Most of the timber that we harvest comes from Crown tenures, and insurance coverage is maintained only for loss of logs due to fire and other occurrences following harvesting. However, this coverage does not extend to standing timber, and there is no assurance that our coverage would be adequate to provide protection against all eventualities, including natural catastrophes.

In addition, our operations may be adversely affected by fluctuations in the water levels in Williston lake as well as severe weather including wind, snow and rain that may result in our operations being unable to harvest or transport logs to the Mackenzie mill. We are unable to predict the impact of all these factors on our tenures or our forest practices.

While we maintain insurance coverage which we believe is standard in our industry, we cannot predict that all potential insurable risks have been foreseen or that adequate coverage is maintained against known risks. As is common in our industry, we do not insure loss of standing timber for any cause.

Forest Health

The Mountain Pine Beetle ("MPB") infestation is believed to have largely run its course. However, the MPB infestation's impact on our operations remains uncertain. The potential effects include a reduction in future AAC levels to below current and pre-MPB AAC levels, a diminished grade and volume of lumber recoverable from MPB-killed logs, decreased quality of wood chips produced from such logs and increased production costs. The Chief Forester of British Columbia has begun reducing the AAC's of the MPB impacted TSAs and we expect this trend to continue in the foreseeable future. The containment or further spread of the MPB infestation will depend on a number of factors including the harvesting of timber in MPB infested areas and weather conditions.

The Mackenzie TSA has seen an outbreak of spruce beetle. We therefore expect to shift harvesting into timber stands that are under imminent threat or have a high susceptibility to beetle infestation. Together with the Ministry of Forests and other forest companies in the region, we are working to develop strategies to limit any damage caused by the spruce beetle.

A number of different tactics are being employed to mitigate the spread of the spruce beetle, and the impact on our operations appears to be manageable at this time. However, the timing and extent of the effect on our timber supply, lumber grade and recovery, wood chip quality and production costs by both the MPB and spruce beetle will depend on a variety of factors which cannot be determined at this time with any certainty.

Environment

Our operations are subject to regulation by federal, provincial, state, municipal and local environmental authorities, including industry specific environmental regulations, permits, guidelines and policies relating to air emissions and pollutants, wastewater discharges, solid waste, landfill operations, clean-up of unlawful discharges, dangerous goods and hazardous materials, forestry practices, land use planning, municipal zoning, employee health and safety, site remediation and the protection of endangered species and critical habitat. In addition, as a result of our operations, we may be subject to remediation, clean-up or other administrative orders or amendments to our operating permits, and we may be involved from time to time in administrative and judicial proceedings or inquiries. Future orders, proceedings or inquiries could have a material adverse effect on our business, financial condition and results of operations. Environmental laws and land use laws and regulations are constantly changing. New regulations or the increased enforcement of existing laws could have a material adverse effect on our business and financial condition. In addition, compliance with regulatory requirements is expensive, at times requiring the replacement, enhancement or modification of equipment, facilities or operations. There can be no assurance that we will be able to maintain our profitability by offsetting any increased costs of complying with future regulatory requirements.

We are subject to liability for environmental damage at the facilities that we own or operate, including damage to neighbouring landowners, residents or employees, particularly as a result of the contamination of soil, groundwater or surface water and especially drinking water. The costs of such liabilities can be substantial. Our potential liability may include damages resulting from conditions existing before we purchased or operated these facilities. We may also be subject to liability for any offsite environmental contamination caused by pollutants or hazardous substances that we or our predecessors arranged to transport, store, treat or dispose of at other locations. In addition, we may be held legally responsible for liabilities as a successor owner of businesses that we acquire or have acquired. The Mackenzie mill has been operating for decades, and we have not done invasive testing to determine whether or to what extent any such environmental contamination exists. As a result, there may be liabilities for conditions that we discover or that become apparent, including liabilities arising from non-compliance with environmental laws by prior owners. Because of the limited availability of insurance coverage for environmental liability, any substantial liability for environmental damage could materially adversely affect our results of operations and financial condition.

We have in place internal programs under which our forestry and manufacturing operations are audited for compliance with environmental laws and accepted standards and with our management systems. Our woodlands operations and the harvesting operations of our key suppliers are third party certified to internationally-recognized sustainable forest management standards. Our operations and our ability to sell products could be adversely affected if those operations did or do not, or were perceived by the public as failing to, comply with applicable laws and standards, including responsible environmental and sustainable forestry standards.

Enactment of new environmental laws or regulations or changes in existing laws or regulations might require significant capital expenditures. We may be unable to generate sufficient funds or to access other sources of capital to fund unforeseen environmental liabilities or expenditures.

Stumpage Fees

Substantially all of our log requirements at our Mackenzie mill are harvested from Crown lands in British Columbia. The Province of British Columbia charges stumpage fees to companies that harvest timber from Crown land. Stumpage fees for a specific harvesting area are based on a competitive Market Pricing System ("MPS") that has been established for the interior region of British Columbia. The stumpage system is complex and the subject of discussion involving, among other things, lumber trade agreements between Canada and the United States. The primary variable in the MPS is log pricing established through an open market auction for standing timber administered by BC Timber Sales. In addition to bid prices, there are a number of operational and administrative factors that will influence an individual stumpage rate for each cutting permit. Stumpage rates are also adjusted quarterly to reflect changes in lumber prices.

Periodic changes in the provincial government's administrative policy can affect the market price for timber and the viability of individual logging operations. There can be no assurance that current or future changes will not have a material impact on stumpage rates.

Aboriginal Claims

Canadian court decisions have recognized the existence of Aboriginal title and rights, which may include title or rights of use to lands historically used or occupied by Aboriginal groups. Aboriginal groups have claimed Aboriginal rights and/or title over a significant portion of British Columbia, and few treaties are in place between the Crown and Aboriginal groups in British Columbia. While certain Aboriginal groups in British Columbia have entered into treaty negotiations with the Crown, such negotiations involve complex issues that may take many years to resolve, if at all, and the results of such negotiations cannot be predicted.

Courts have held that the Crown has an obligation to consult with Aboriginal groups when the Crown has knowledge of either existing rights or the potential existence of Aboriginal title or rights and is contemplating actions that may potentially impact such title or rights. Failure of the Government of British Columbia to adequately discharge its obligations to Aboriginal groups may affect the validity of its actions in dealing with public rights, including the granting of Crown timber harvesting rights.

In 2014, the Supreme Court of Canada ("**SCC"**) released the *Tsilhqot'in v. British Columbia* decision in which for the first time the SCC recognized the existence of Aboriginal title over land in British Columbia. The SCC also found that provincial laws of general application may apply to land subject to Aboriginal title, provided that certain conditions are met, including that the laws are not unreasonable, impose no undue hardship and do not deny the holders of such Aboriginal title of certain rights. As a result, future court decisions may be required to determine whether and to what extent provincial laws, including the Forest Act and licences granted by the Provincial Crown thereunder, apply on lands subject to Aboriginal title. While Aboriginal title has not been established or formally recognized in areas overlapping with our forest tenures, there can be no assurance that Aboriginal title will not in the future be recognized over all or any portion of the area covered by our forest tenures. We cannot assure that Aboriginal claims will not in the future have a material adverse effect on our timber harvesting rights, our ability to exercise or renew them or our ability to secure other timber harvesting rights.

Additionally, the Canadian Federal government and the Province of British Columbia have made commitments to review their relationships with aboriginal groups, British Columbia has adopted United Nations Declaration on the Rights of Indigenous Peoples ("**UNDRIP**") and the Canadian Federal government has expressed its support for UNDRIP. At this time, we are unable to assess the effect, if any, that the adaption and implementation of UNDRIP may have on land claims and consultation requirements, but the impact may be material.

Labour Relations

Production disruptions resulting from walkouts or strikes by unionized employees could result in lost production and sales, which could have a material adverse impact on our business We employ a unionized work force in our sawmilling and power generation operations. In 2019, our union employees at the Mackenzie mill ratified a new, five-year collective labour agreement with the USW. Subsequent to year end, in January 2020, our union employees at the Mackenzie power plant also ratified a new, five-year collective labour agreement with the USW. Both agreements are retroactive to July 1, 2018 and expire on June 30, 2023. We believe our current labour relations are stable and do not anticipate any significant related disruptions to our operations in the foreseeable future.

We also depend on a variety of third parties that employ unionized workers to provide critical services. Labour disputes experienced by these third parties could lead to disruptions at our facilities.

Maintenance Obligations and Facility Disruptions

Our manufacturing processes are vulnerable to operational problems that could impair our ability to manufacture products. We could experience a breakdown in any of our machines or other important equipment, and from time to time, planned or unplanned maintenance outages that cannot be performed safely or efficiently during normal hours of operation. Such disruptions could cause a loss of production, which could potentially have a material adverse effect on our business, financial condition and operating results.

Periodic Litigation

We may from time to time become party to claims and litigation proceedings that arise in the ordinary course of business. Such matters are subject to many uncertainties, and we cannot predict with assurances the outcomes and ultimate financial impacts of them. There can be no guarantees that actions that may be brought against us in the future will be resolved in our favour or that the insurance we carry will be available or paid to cover any litigation exposure. Any losses from settlements or adverse judgments arising out of these claims could be materially adverse to us.

Tax Exposures

In the normal course of business, we take various tax filing positions without the assurance that tax authorities will accept and not challenge such positions. In addition, we are subject to further uncertainties concerning the interpretation and application of tax laws in various operating jurisdictions. We maintain reserves for known estimated tax exposures in all jurisdictions. These exposures are settled primarily through the closure of audits with the jurisdictional taxing authorities.

OUTSTANDING SECURITIES

As at March 1, 2021, we had 46,457,030 common shares, 2,069,875 long-term incentive plan awards and 3,500,000 warrants outstanding.

EVALUATION OF INTERNAL CONROLS AND DISCLOSURE CONTROLS AND PROCEDURES OVER FINANCIAL REPORTING

In accordance with the requirements of *National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings* (NI 52-109), the Company's management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), has evaluated the effectiveness of the Company's internal control over financial reporting. Management of Conifex is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, the CEO and CFO, and it is effected by management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2020 and management believes that the Company's internal control over financial reporting were effective. Management's assessment was based on the framework established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, the CEO and CFO have concluded that Conifex's internal control over financial reporting, as defined in NI 52-109, is designed and operating effectively. In addition, the CEO and CFO confirm that there were no changes in the controls which materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting during the year ended December 31, 2020.

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the CEO and CFO, on a timely basis so that appropriate decisions can be made regarding annual and interim filings or other disclosure. An evaluation of the effectiveness of the design and operation of disclosure controls and procedures was conducted as of December 31, 2020 by Conifex's management, including the CEO and CFO. Based on this evaluation, the CEO and CFO have concluded that Conifex's disclosure controls and procedures, as defined in NI 52-109, were effective as of December 31, 2020.

ADDITIONAL INFORMATION

Additional information about our company is available on SEDAR at www.sedar.com.