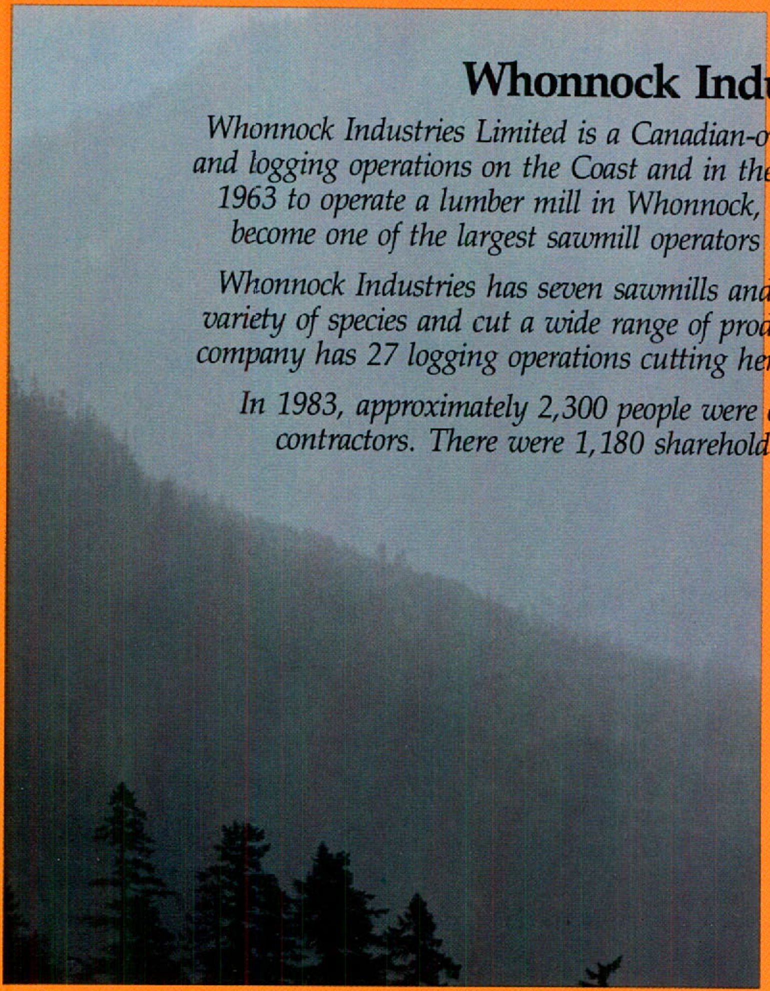
Whonnock Industries Limited Annual Report 1983



Whonnock Industries Limited

Whonnock Industries Limited is a Canadian-owned forest products company with sawmills and logging operations on the Coast and in the Interior of British Columbia. Incorporated in 1963 to operate a lumber mill in Whonnock, B.C., the company has expanded rapidly to become one of the largest sawmill operators and lumber exporters in British Columbia.

Whonnock Industries has seven sawmills and a shake and shingle plant. The mills use a variety of species and cut a wide range of products, many of which are custom orders. The company has 27 logging operations cutting hemlock, balsam, fir, cedar, cypress and spruce.

In 1983, approximately 2,300 people were employed by Whonnock Industries and its contractors. There were 1,180 shareholders of record as of December 31, 1983.

Financial Summary

	12 months ended	
INCOME STATEMENT	**December 31, 1983**	December 31, 1982
Sales	**$ 269,612,000**	$ 224,324,000
Operating Margin (before interest)	**11,492,000**	(7,799,000)
(Loss) before extraordinary item	**(1,934,000)**	(21,189,000)
Net Income (Loss) for the year	**4,746,000**	(21,189,000)
Earnings (Loss) per share	**0.73**	(3.44)
BALANCE SHEET	**December 31, 1983**	December 31, 1982
Working Capital	**$ 26,003,000**	$ 17,416,000
Total Assets	**218,948,000**	210,626,000
Total Equity	**38,620,000**	33,874,000
Equity per share	**5.95**	5.22

Sales reached a record $270 million in 1983, reflecting a strong demand in North American lumber markets. A 17% increase in lumber volumes combined with a 9% increase in prices resulted in a $20 million turnaround from last year's operating margins.

REPORT FROM THE CHAIRMAN

This past year has again been one of difficult challenges, but also one of considerable satisfaction. Although our dominant market areas showed no major improvement in 1983, lumber sales increased by 26%, resulting in record total sales of $270 million compared to $223 million in 1982.

Operating margins (measured before interest) improved by almost $20 million, largely as a result of the improvement in sales volumes.

Net earnings for the year reached $4.7 million compared to a loss of $21.2 million in 1982. Included in the earnings for 1983 is an extraordinary gain of $6.7 million, resulting from an agreement to terminate the Bay Forest Products land lease two years early. The Bay land was required to permit the construction of facilities for Expo 86.

Our overall financial position improved considerably this year. In this year's review of operations, we have described a rather complex but successful refinancing of Western Forest Products Limited. The refinancing, which involves substantial new equity and a very necessary pulp mill rebuild, considerably improves the outlook for this investment. This improved security of our investment enables us to plan more effectively based on a secure timber supply from Western Forest Products and a future direct participation in the pulp business.

There are other strengths in our financial position that are not completely obvious from the financial statements. Our bank loans are $16 million below our authorized lines of credit which is an improvement of approximately $6 million from 1982. The company's tax position provides the ability to generate a substantial cash flow that is considerably in excess of profits. We have estimated that the company can earn $55 million without paying current taxes.

Another strength of our company, of which I am the proudest, is our people. We have tried to provide an environment that encourages our employees to realize their full potential. The entrepreneurial spirit that has resulted is most gratifying. I deeply appreciate the support of our employees, management and directors during these uncertain economic times.

On a sadder note, I report the passing of Murray H. MacKenzie in June of 1983. Murray was Chairman and a Director of Whonnock Industries for many years. His skills and advice will be greatly missed, as well as his cheerful optimism.

As a result, I have become Chairman and Chief Executive Officer and John C. Southcott has become President and Chief Operating Officer.

During 1983, capital expenditures were again kept to a minimum with an emphasis on efficiency improvements that would result in a rapid investment pay back. This policy will continue in 1984 except for the replacement of the former Bay Forest Products lumber manufacturing capacity.

On March 31, Whonnock will take over the Pitt Meadows sawmill, formerly owned by CIPA Industries, a company controlled by C. Itoh & Co. Ltd. of Japan. The exact financial structure of this transaction has not yet been finalized.

The sawmill, although modern and in excellent condition, will be adapted to Whonnock's customer requirements and long-term log supply at an additional cost of approximately $5 million. The overall cost, however, will be very attractive when compared to the alternative of building a new mill.

The outlook for 1984 is for continued strengthening of our industry. Lumber prices in the North American markets have already begun a slow firming. Overseas markets show signs of improvement for the second half of the year. The strengthening of pulp markets indicates higher by-product selling prices as the year progresses.

While we do not expect the recovery to be rapid or completely constant, we now look forward to an extended period of modest prosperity.

On behalf of the board of directors,

W. L. Sauder

William L. Sauder
Chairman and Chief Executive Officer

HEALTHY PERFORMANCE IN A DIFFICULT YEAR

Operating margins recovered substantially in 1983. Higher production levels and increased productivity, combined with increased selling prices, resulted in a $20 million turnaround from 1982.

An extraordinary item also had a significant effect on the Income Statement. The Bay Forest Products mill in the False Creek area closed on December 31, 1983 to make way for Expo 86 development. Whonnock Industries received a cash settlement as compensation for leaving the site two years before the lease expired. The settlement took into account expected profits for the years 1984 and 1985. After costs for severance pay and losses on the disposal of buildings and equipment, net proceeds were approximately $6.7 million.

For the second time a stock dividend was issued in order to preserve the company's shares as pension plan and other regulated investments without reducing working capital. The Class A stock dividend was 1.5% and the Class B stock dividend was 0.29%. Based on a share price of $11.00, the cash equivalents of these dividends per share were $16\frac{1}{2}$¢ and $3\frac{1}{6}$¢ respectively.

An investment in pulp

The refinancing of Western Forest Products Limited (WFP), completed in December 1983, has greatly improved the strength and viability of our investment in that Company. Although WFP's operating results have been similar to most other forest products companies, its capital structure was not designed to withstand an extended recession.

There were two basic facets of the refinancing to strengthen the operations. First,

Whonnock Industries controls or has direct access to approximately 10% of the British Columbia coast's annual timber supply. Hemlock, balsam and western red cedar are the main species cut.

the debt of WFP had to be reduced in order to reduce interest costs. Second, the rebuild of the Squamish pulp mill had to be completed to make the mill cost-competitive with other mills. The first is now completed and the second is underway.

Approximately 60% of WFP's term debt was converted to equity through the issue of $100 million in common shares and $144 million in preferred shares to WFP's bankers. Of the preferred shares, $30 million carry voting rights. In 1986, Whonnock will be required to begin purchasing $10 million of the voting preferred shares at an annual rate equal to the lesser of $2.5 million and 20% of our net income for the previous year. Although this reorganization will initially reduce Whonnock's voting rights from 33.3% to 19.5%, the value of the investment will actually increase as a result of the equity increase.

An analysis of the cost to rebuild the Squamish mill demonstrated that the viability of the project would be greatly enhanced if WFP were able to utilize the income tax incentives available for such projects. Since neither WFP nor their original owners were able to immediately benefit from these incentives, a method was needed that could transfer these benefits to a new group of equity investors. To meet that requirement, the Western Pulp Limited Partnership was formed to acquire both of WFP's pulp mills, to rebuild the Squamish mill at a cost of approximately $215 million and to enhance the Port Alice pulp mill at a cost of $15 million. The Partnership raised $110 million in new equity funds during December 1983 which, together with a bank credit of $150 million, ensured that the rebuild could begin immediately.

As consideration for selling the pulp mills to the Partnership, WFP holds a debenture that is convertible into an approximate 60% share of the Partnership by 1996. After 1986, Partnership unit holders can elect to exchange their units for shares of Whonnock, Doman Industries Limited and B.C. Forest Products Limited. If the exchange is completed, WFP and its shareholders will once again own the pulp mills, but on a much stronger financial base. Furthermore, upon such an exchange it is expected that Whonnock Industries would issue approximately two million shares at $17.63 per share. This would increase our equity by $35 million and give us a direct involvement in the pulp business.

Second in lumber; third in timber

Whonnock Industries has grown by 50% since 1979. During 1983, we were the second largest coastal lumber producer and had, including Whonnock's portion of WFP's timber, the third largest timber position on the coast.

Our timber reserves include large tracts of old growth cedar which is used for many premium lumber products.

Seaboard is one of the world's largest lumber exporters. Whonnock is its largest shareholder.

Seaboard has been particularly successful in developing new markets in Japan, North Africa and China.

Mills working at capacity

Lumber production in 1983 was at a record high volume. We achieved this despite a two-month closure of Silvertree at the beginning of the year.

This successful operating year is a result of our employees' efforts. Lumber recovery levels improved at all mills and costs were held below 1982 levels.

As part of our continuing program to improve productivity and lumber recovery, in late 1982 we installed a "state of the art" trimmer optimizer at Holding Lumber. Its benefits became very apparent with its first full year of use, when lumber recovery improved by 15 percent.

Including Bay, we operated seven sawmills and a shake and shingle mill. The mills have a combined two-shift capacity of over 600 million board feet per year and employ 1,400 people.

Although this was another difficult year for the industry as a whole, we are pleased to report that we cut almost 100% of our timber quota. This meant that most of our 27 logging operations worked at full capacity throughout the year.

Two important reasons for our improved performance are that productivity has increased and costs were held down. We have also achieved a breakthrough in controlling log inventory by anticipating and responding more quickly to changing market demands.

The new emphasis on employee involvement and group decision-making in our logging safety program is showing results.

Despite the need for cost control at all levels of the company, we continued to emphasize long-range timber planning. We stepped up our reconnaissance work and have strengthened our timber base as a result. One small crew does all the timber cruising (inventory-taking) for the company. Their work has been of consistently high quality.

Although not a record, we planted slightly more than two million trees this year.

Our logging operations are situated in the coast region from Hope to Prince Rupert and in the Interior at Adams Lake. We cut mainly hemlock-balsam, followed, in descending volumes, by western red cedar, Douglas fir, spruce and cypress.

Predicting markets, maximizing sales

Early in the year, we anticipated an increased demand for cedar and changed our logging plans accordingly. We responded quickly enough to take full advantage of the stronger markets.

Each of our seven sawmills is responsible for its own sales. They cut for specific markets and meet special customer needs.

Added to this flexibility is the collective marketing expertise of Seaboard Lumber Sales Company and Seaboard Shipping Company. These companies sell and ship our products to markets overseas and to the U.S. East Coast. Largely due to their successful marketing, we were able to keep all our mills running at increased production levels despite the difficult year.

Seaboard is one of the world's largest lumber exporters. It is owned by 20 B.C. forest companies, with Whonnock Industries the largest shareholder. In 1983, Seaboard received the Canada Export Award for its outstanding achievement in foreign trade.

Lumber sales up 26% in 1983

Prices fluctuated significantly during the year, in step with the shifting market forces of supply and demand. However, with the overall price average up by about 9% and a 17% increase in our volumes, Whonnock's lumber sales exceeded the $250 million mark for the first time in our history.

By-product volumes were up correspondingly, but the selling price of chips continued to slide. Prices dropped by approximately 30% for the second year in a row. This trend seems to have reversed, however, and we forecast higher prices in 1984.

Our major markets are overseas. The devaluation of the Swedish krona has made our products less competitive in Europe, but this is offset by other markets on the Pacific Rim and in North Africa. We continue to increase our sales to China.

The entrepreneurial approach towards marketing and profit opportunities resulted in the expansion of our custom cutting program. With our mills operating at capacity, we used other mills to cut our logs, particularly western red cedar and spruce.

Diversified markets the key

Our strategy to diversify markets has shown benefits during a recession such as this one in 1982-83. Although the recession has been worldwide, it has affected different countries at different times and for varying periods. Therefore, if one of our markets is weak, others, coming out of the recession, are often stronger.

We are not dependent on any one market, and that is a major strength. Our total company production is planned in such a way that not more than 20% is geared to any single market. This provides us with greater security but still enables us to take advantage of current market trends.

Employee efforts pay off

Throughout the company, productivity increased. This is due partly to some equipment purchases, but mainly to our employees' commitment and desire to keep their company competitive at all times. Their efforts were very much needed and are greatly appreciated.

Capital expenditures again were restricted to essential replacements and to several minor opportunities with a rapid pay back. A major item was the introduction of two grapple yarders. They are part of our continuing program to improve our logging capability by replacing spars. Although expansion programs have been avoided, improvements in efficiency have been very worthwhile.

Lumber production in 1983 was at a record high volume.

Our mills have the ability to produce many sizes and grades of lumber to meet individual customer needs.

Developing leaders

Decentralized decision-making and small operational units encourage initiative and entrepreneurship at all levels of the company. With this organization, complemented by strong training and recruiting, we are poised for recovery and expansion.

Strength in timber holdings

Whonnock's timber position is excellent. We log approximately 1.9 million cubic metres and we have direct access to a further 800,000 cubic metres through WFP and B.C. Forest Products. This represents about 10% of the annual coastal timber supply. Our production in the Interior exceeds 400,000 cubic metres per year.

Solid future for growth

Since its formation in 1963, Whonnock Industries has expanded to become one of the largest sawmillers and lumber exporters in British Columbia.

Our investment in Western Pulp Limited Partnership represents a major step in our plans to become an integrated resource company.

Markets on every continent produced 1983 sales of $270 million.

Company assets total $219 million.

The combined strengths of our timber position, productive mills and logging operations, highly skilled employees and the expertise of our marketing firm are immeasurable assets.

We are building on this solid foundation.

Including its one third share of Western Forest Products, Whonnock Industries has the third largest timber position on the coast. In 1983, Whonnock again harvested close to 100% of its annual cutting rights.

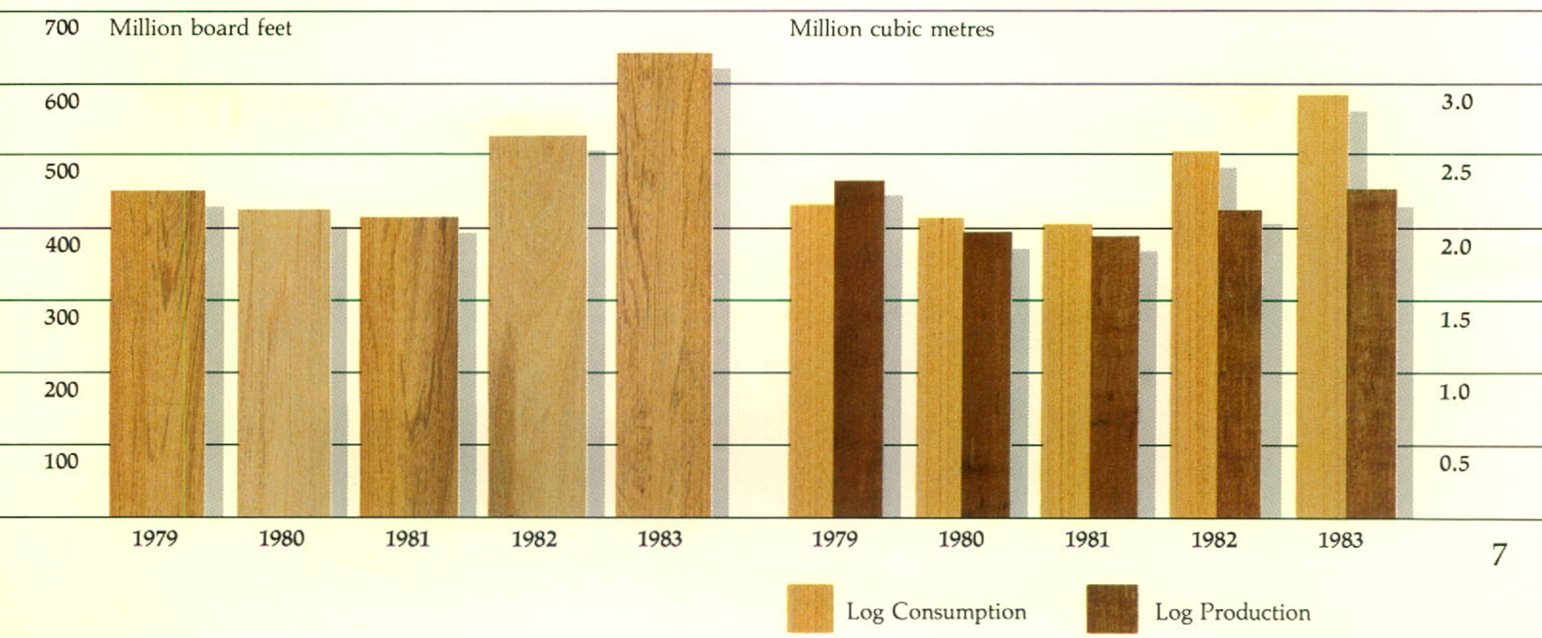
Five Year Review

		1983	1982	1981	1980	1979
PRODUCTION STATISTICS						
Lumber (Million FBM)		**641**	529	415	424	445
Logs (Thousand cubic metres)		**2,365**	2,200	1,925	1,958	2,316
EMPLOYEE STATISTICS						
Wages, salaries	($000)	**65,503**	58,929	42,829	39,218	34,855
Number of employees		**2,081**	1,895	1,835	1,590	1,610
FINANCIAL STATISTICS						
Sales	($000)	**269,612**	224,324	174,692	190,565	190,845
Stumpage	($000)	**9,320**	8,212	9,270	21,143	19,057
Income taxes (recovery)	($000)	**(2,600)**	(11,148)	(8,130)	8,030	18,008
Net income (loss)	($000)	**4,746**	(21,189)	(9,408)	11,244	22,877
Earnings (loss) per share*	$	**0.73**	(3.44)	(1.53)	1.83	3.72
Total assets	($000)	**218,948**	210,626	217,683	181,872	114,314
RATIO AND INVESTMENT INFORMATION						
Current Ratio		**1.5:1**	1.4:1	1.4:1	1.5:1	1.4:1
Equity per common share*	$	**5.95**	5.22	8.21	10.01	8.36
Share price range - high	$	**12.00**	9.00	16.75	15.38	11.50
- low	$	**6.38**	2.20	5.75	7.13	4.00
Price/Earnings ratio		**16.4**	—	—	8.0	2.9
RE-INVESTMENT						
Working capital generated from (applied to) operations	($000)	**11,932**	(14,182)	(862)	24,800	33,913
Plant, equipment and roads	($000)	**11,240**	12,344	32,543	16,554	23,035
Working capital retained		**692**	(26,526)	(33,405)	8,246	10,878

*Stock dividends applied retroactively.

LUMBER PRODUCTION

LOG PRODUCTION



Consolidated Balance Sheet as at December 31, 1983

(Thousands of Dollars)

ASSETS

	1983	1982 (As restated - note 2)
CURRENT ASSETS		
Trade and other accounts receivable	$ 16,938	$ 11,783
Inventories (note 3)	56,868	50,057
Prepaid expenses	1,668	1,328
	75,474	63,168
INVESTMENTS AND OTHER ASSETS		
Investments and advances	3,060	2,214
Timber sale deposits	741	621
Investment in Western Forest Products Limited (note 4)	58,400	59,420
	62,201	62,255
FIXED ASSETS		
Property, plant and equipment, at cost (note 5)	82,823	84,998
Less accumulated depreciation	37,089	32,453
	45,734	52,545
Timber, at cost less accumulated depletion	10,221	10,698
Logging roads, at cost less accumulated amortization	14,374	13,472
	70,329	76,715
DEFERRED CHARGES		
Deferred financing fee, net of accumulated amortization	1,444	1,588
Deferred income taxes (note 6)	9,500	6,900
	10,944	8,488
	$218,948	$210,626

Approved by the Board

G. L. Sauder Director

J. T. Southcott Director

LIABILITIES

	1983	1982 (As restated - note 2)
CURRENT LIABILITIES		
Bank indebtedness (note 7)	$ 21,586	$ 27,522
Accounts payable and accrued liabilities	26,736	18,130
Principal due within one year on long-term debt (note 7)	1,149	100
	49,471	45,752
LONG-TERM DEBT (note 7)	130,857	131,000

SHAREHOLDERS' EQUITY

	1983	1982
CAPITAL STOCK (note 8)		
Issued and fully paid		
5,829,108 class A subordinate voting shares	10,954	10,006
661,808 class B common shares	450	429
6,490,916	11,404	10,435
RETAINED EARNINGS	27,216	23,439
	38,620	33,874
	$218,948	$210,626

Commitments and contingent liability (note 9)

Auditors' Report

To the Shareholders of
Whonnock Industries Limited

We have examined the consolidated balance sheet of Whonnock Industries Limited as at December 31, 1983 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at December 31, 1983 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied, after giving retroactive effect to the change in the method of determining inventory values as explained in note 2 to the financial statements, on a basis consistent with that of the preceding year. This change, with which we concur, had no material effect on the 1983 and 1982 operating results.

Vancouver, Canada
February 16, 1984

Thorne Riddell
Chartered Accountants

Consolidated Statement of Income

year ended December 31, 1983
(Thousands of Dollars)

	1983	1982
SALES	$269,612	$224,324
COSTS AND EXPENSES		
Production	231,175	205,533
Selling and administration	10,549	11,165
Depreciation	8,205	8,208
Depletion and amortization	8,191	7,217
Interest on long-term debt	12,184	15,515
Other interest	4,104	6,545
	274,408	254,183
OPERATING LOSS	4,796	29,859
OTHER INCOME	262	565
	4,534	29,294
EQUITY IN LOSS FROM WESTERN FOREST PRODUCTS LIMITED (note 1[c])	—	3,043
LOSS BEFORE INCOME TAXES AND EXTRAORDINARY ITEM	4,534	32,337
DEFERRED INCOME TAX REDUCTION	2,600	11,148
LOSS BEFORE EXTRAORDINARY ITEM	1,934	21,189
EXTRAORDINARY ITEM		
Settlement on termination of Bay Forest Products land lease, net of closing costs, severance payments and income taxes	6,680	—
NET INCOME (LOSS)	$ 4,746	$ (21,189)
EARNINGS (LOSS) PER SHARE (note 10)		
Loss before extraordinary item	$ (.30)	$ (3.44)
Net income (loss)	$ .73	$ (3.44)

Consolidated Statement of Retained Earnings

year ended December 31, 1983
(Thousands of Dollars)

	1983	1982
BALANCE AT BEGINNING OF YEAR, as restated (note 2)	$ 23,439	$ 45,714
Net income (loss)	4,746	(21,189)
	28,185	24,525
Less stock dividends		
Class A subordinate voting shares	948	1,049
Class B common shares	21	37
	969	1,086
BALANCE AT END OF YEAR	$ 27,216	$ 23,439

Consolidated Statement of Changes in Financial Position

year ended December 31, 1983
(Thousands of Dollars)

	1983	1982
WORKING CAPITAL DERIVED FROM		
Operations		
Loss before extraordinary item	$ 1,934	$ 21,189
Items not involving working capital	13,866	7,007
Cash flow (loss) from operations	11,932	(14,182)
Disposal of property, plant and equipment	832	416
Increase in long-term debt	1,006	21,000
Issuance of capital stock	—	1,543
Net proceeds on termination of Bay Forest Products land lease	8,446	—
	22,216	8,777
WORKING CAPITAL APPLIED TO		
Property, plant and equipment	3,788	4,500
Logging roads	7,452	6,848
Timber	—	996
Investments and other assets	1,240	303
Reduction in long-term debt	1,149	100
Deferred financing fee	—	1,600
Investment in Western Forest Products Limited	—	220
	13,629	14,567
INCREASE (DECREASE) IN WORKING CAPITAL	8,587	(5,790)
WORKING CAPITAL AT BEGINNING OF YEAR, as restated (note 2)	17,416	23,206
WORKING CAPITAL AT END OF YEAR	$ 26,003	$ 17,416

Notes to Consolidated Financial Statements

Year Ended December 31, 1983

1. SIGNIFICANT ACCOUNTING POLICIES

(a) Principles of consolidation
The financial statements include the accounts of the wholly-owned subsidiary, Holding Lumber Company Limited.

(b) Inventories
Inventories have been valued at the lower of cost and net realizable value (note 2).

(c) Investment in Western Forest Products Limited
The investment in Western Forest Products has been accounted for on the cost basis since January 31, 1982.

Interest on the funds borrowed for the acquisition during the initial six month period of planning and orientation is included in the carrying value of the investment and is being amortized over a five year period commencing November 1, 1981.

(d) Depreciation, amortization and depletion
Depreciation of plant and equipment is provided on a straight-line basis during periods of production at rates (ranging from 5% to 20%) based on the estimated useful lives of the fixed assets. Depletion and road amortization are computed on the basis of timber cut. Amortization of the deferred financing fee is provided over the term of the related bank loans.

2. CHANGE IN ACCOUNTING POLICY

During the year the company modified the basis of applying the principle of lower of cost and net realizable value for inventories from an individual item by item basis to a determination by major product groupings for each division. This new basis conforms more closely to industry practice and will reduce the distortive effect of seasonal volume fluctuations.

This change in application has been applied retroactively, increasing retained earnings and inventories by $3,039,000 as at December 31, 1981.

The change had no material effect on the operating results for 1983 and 1982.

3. INVENTORIES

	1983	1982
	(Thousands of dollars)	
Logs	$41,954	$40,499
Lumber	14,359	9,030
Other	555	528
	$56,868	$50,057

4. INVESTMENT IN WESTERN FOREST PRODUCTS LIMITED

(a) The investment in Western Forest Products Limited (WFP) consists of the following components:

	1983	1982
	(Thousands of dollars)	
Balance, beginning of year	$59,420	$62,515
Interest deferred during Squamish pulpmill rebuild	—	220
	59,420	62,735
Equity in after-tax loss of WFP (see note 1 [c])	—	(2,295)
Amortization of initial six-month deferred interest	(1,020)	(1,020)
Balance, end of year	$58,400	$59,420

(b) Condensed consolidated financial information for WFP at its year end October 31, 1983 is as follows:

WESTERN FOREST PRODUCTS LIMITED

Balance Sheet — October 31, 1983

(Thousands of dollars)

NET ASSETS	Pro forma 1983	1983	1982
Working capital (deficiency)	$ 43,722	$(395,179)	$(356,718)
Investment in Western Pulp Limited Partnership	175,242	—	—
Fixed assets	238,564	401,077	411,144
Other assets, net	45,675	58,404	50,815
	$ 503,203	$ 64,302	$ 105,241
LIABILITIES AND SHAREHOLDERS' EQUITY			
Long-term debt	$ 195,000	$ —	$ —
Capital stock	423,901	180,000	180,000
Deficit	(115,698)	(115,698)	(74,759)
	$ 503,203	$ 64,302	$ 105,241

The pro forma condensed balance sheet gives effect to the transactions described in (c) below as though they had occurred on October 31, 1983.

For the year ended October 31, 1983, WFP incurred losses of $40,939,000 (1982 — $61,124,000) on sales of $227,801,000 (1982 - $211,126,000).

(c) The reorganization of WFP, completed in December 1983, consisted of the following two steps:

i) Approximately 60% of WFP's term debt was converted to equity by the issuance to WFP's bankers of $100,000,000 in common shares and $143,901,000 in preferred shares.

ii) The Western Pulp Limited Partnership was formed to acquire both of WFP's pulp mills. The Partnership raised the $110,000,000 in new equity required to finance the rebuild of the Squamish mill and improvements to the Port Alice mill.

Although the reorganization reduced Whonnock's voting interest from 33.3% to 19.5%, Whonnock's interest in the underlying net book value of WFP's assets as reflected on the pro forma balance sheet improved.

The refinancing of WFP is supportive of Whonnock's view that there has been no permanent decline in value of the investment.

Whonnock has not guaranteed any bank loans or other liabilities of WFP.

5. PROPERTY, PLANT AND EQUIPMENT

	1983 (Thousands of dollars)			1982
	Cost	Accumulated depreciation	Net	Net
Land	$10,179	—	$10,179	$ 9,718
Buildings	14,531	$ 5,983	8,548	8,940
Machinery and equipment	46,296	24,466	21,830	26,650
Automotive equipment	6,080	4,279	1,801	2,329
Other	5,737	2,361	3,376	4,908
	$82,823	$37,089	$45,734	$52,545

6. INCOME TAXES

The company reflects as an asset only the future tax benefit related to recording depreciation, amortization and depletion in excess of the amount claimed for tax purposes. Additional future tax benefits in excess of those recorded which arise from operating losses are also available. During the year, the company utilized a portion of these losses leaving a balance of $3,600,000 available to reduce future years' income taxes. In addition, the company has not recorded the benefit of investment tax credits totalling $615,000 which are available for periods of three to five years.

7. LONG-TERM DEBT

	1983	1982
	(Thousands of dollars)	
Bank term loan, Toronto Dominion Bank, with the first repayment due in 1985	$ 117,000	$ 97,000
Bank term loan, with first repayment due in 1984	4,000	3,000
Short-term bank indebtedness, with term refinancing in place	10,000	31,000
Obligations under capital lease and purchase agreements	1,006	100
	132,006	131,100
Less principal included in current liabilities	1,149	100
	$ 130,857	$ 131,000

Term bank loans with the Toronto Dominion Bank bear interest at the bank prime plus 5/8% or, at the company's option, at a rate fixed for varying periods for Banker's Acceptances.

Bank indebtedness and term bank loans are secured by accounts receivable, inventories, the shares in WFP and a debenture.

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

1984	$ 1,149,000
1985	7,658,000
1986	10,666,000
1987	12,603,000
1988	12,566,000

The Agreement covering this debt contains provisions which (a) may vary the principal instalments due in future years, dependent upon amounts of working capital, cash flow from operations, capital expenditures and proceeds from major disposal of assets; and (b) require the prior consent of the lenders for the payment of cash dividends.

8. CAPITAL STOCK

Authorized capital consists of:

15,400,000 class A subordinate voting shares without par value
4,600,000 class B common shares without par value
5,000,000 preference shares without par value

Share transactions during the year:

	Number		
	Class A	Class B	Amount
Balance at beginning of year	5,742,965	659,908	$10,435,000
Stock dividend*	86,143	1,900	969,000
Balance at end of year	5,829,108	661,808	$11,404,000

*at $11.00 per share.

The first 13⅓¢ per share per annum of any dividends declared are paid on the class A shares. Any additional dividends shall be declared in equal amounts on the class A and B shares.

The class B shares (carrying ten votes per share) are exchangeable into class A shares (carrying one vote per share) at any time at the option of the holder, on the basis of one class A share for one class B share. Class A shares are reserved for possible future issuance as follows:

(a) 661,808 class A shares are reserved for the conversion of class B shares;

(b) 2,080,379 class A shares are reserved for possible issuance to holders of Western Pulp Limited Partnership units at a price of $17.63 per share in exchange for their partnership units.

9. COMMITMENTS AND CONTINGENT LIABILITY

(a) Commitments

i) The company is obligated under various operating leases requiring minimum annual rental payments in each of the next five years as follows:

1984	$3,035,000
1985	2,867,000
1986	2,744,000
1987	2,609,000
1988	2,215,000

ii) Under the terms of the refinancing agreement entered into by WFP, Whonnock will be required, commencing in 1986, to acquire $10,000,000 of the voting preferred shares at an annual rate equal to the lesser of $2,500,000 or 20% of Whonnock's net income for the previous year.

(b) Contingent liability

Under the terms of the Western Pulp Limited Partnership agreement, Whonnock, Doman Industries Limited, B.C. Forest Products Limited and WFP have agreed, if required, to make revolving loans to the partnership to a maximum of $50,000,000 to cover cash deficiencies that may occur before July 1, 1990. Whonnock's share of the contingent liability is limited to a maximum of $10,000,000 reducing in stages to zero by 1990.

10. EARNINGS (LOSS) PER SHARE

The earnings (loss) per share is calculated using the weighted average number of shares outstanding during the respective fiscal years after giving retroactive effect to the stock dividends.

Fully diluted earnings (loss) per share

Under the terms of the Western Pulp Limited Partnership agreement, class A limited partners have the right to exchange one-third of their class A partnership units for class A subordinate voting shares of Whonnock during the period from April 1987 to June, 1990 at an agreed price of $17.63 per share. Since the value of the partnership units will not be determined until the exchange occurs, it is not possible to determine how many shares will be issued. Although the company expects that the earnings from the partnership will offset the dilution that will occur from the issuance of the shares, maximum fully diluted earnings per share (calculated for 1983 on the basis that the maximum number of shares are issued and no earnings accrue from the investment) are as follows:

Fully diluted earnings (loss) per share	
Loss before extraordinary item	$ (.30)
Net income	$ .55

11. PENSION PLANS

The company contributes to several retirement plans for its employees on a current service basis. These plans are fully funded and there is no unfunded past service liability.

12. RELATED PARTY TRANSACTIONS

The company had net purchases from WFP totalling $38,090,000 (1982 — $25,161,000). Lumber sales to the controlling shareholder in the regular course of business amounted to $3,778,000 (1982 — $1,949,000). These transactions were conducted on a normal commercial basis, including terms and prices. Included as a commitment (note 9[a]) are lease payments to WFP for the Silvertree sawmill lease.

13. OTHER INFORMATION

Remuneration of directors and senior officers of the company amounted to $999,663 (1982 — $984,809).

14. SEGMENTED INFORMATION

The company operates exclusively in the forest products industry and all of its operations are based in Canada.

The company sells to foreign markets, principally through a Canadian sales agency, Seaboard Lumber Sales Company Limited. Sales by major markets are as follows:

	1983				1982
	(Thousands of dollars)				
	Lumber and shakes	Chips and other byproducts	Logs	Total	Total
Canada	$ 43,708	$18,920	$26,707	$ 89,335	$ 64,519
United States	64,759	4,441	—	69,200	47,626
Other export	107,178	—	3,899	111,077	112,179
	$215,645	$23,361	$30,606	$269,612	$224,324

15. COMPARATIVE FIGURES

Certain comparative figures in the income statement have been reclassified to conform with the basis of presentation adopted for 1983, with no effect on the loss for the year.

Whonnock Industries Limited

Head Office
Registered Office

Suite 3500, Bentall Tower Four
1055 Dunsmuir Street
Vancouver, B.C. V7X 1H7
(604) 681-3221

Officers

W.L. Sauder
Chairman and Chief Executive Officer
J.C. Southcott
President and Chief Operating Officer
H.L. Henri
Vice-President
H. Kneteman
Vice-President and Secretary
R.M. Sitter
Vice-President, Forestry and Logging
R.W. Neil
Vice-President, Manufacturing
G.J. Friesen
Vice-President, Finance

Directors

H.L. Henri, Chase, B.C.
A. Holding, Chase, B.C.
H. Kneteman, Vancouver, B.C.
T.E. Lougheed, Penticton, B.C.
R.A.C. McColl, Portland, Oregon
J.A. Milroy, Vancouver, B.C.
W.L. Sauder, Vancouver, B.C.
J.C. Southcott, Vancouver, B.C.

Auditors

Thorne Riddell, Vancouver, B.C.

Transfer Agent

Montreal Trust Company,
Vancouver, B.C.

Log Supply Department

Ste. 3400, Bentall Tower Four 681-3221
1055 Dunsmuir Street
Vancouver, B.C.

Forestry and Logging Group

Ste. 3400, Bentall Tower Four 681-3221
1055 Dunsmuir Street
Vancouver, B.C.

Sawmill Operations

McDonald Cedar Products 888-1616
P.O. Box 69
Fort Langley, B.C. V0X 1J0

MacKenzie Mills 580-1494
11732 - 130th Street
Surrey, B.C. V3R 2Y3

Pacific Pine 525-9411
Ft. of Johnston Street
New Westminster, B.C. V3M 5H6

Silvertree 327-9242
P.O. Box 67339, Stn. "O"
Vancouver, B.C. V5W 3T1

Whonnock Lumber 462-7111
P.O. Box 10,
Whonnock, B.C. V0M 1S0

Whonnock Shake & Shingle 462-7111
P.O. Box 10
Whonnock, B.C. V0M 1S0

Holding Lumber Co. Ltd. 679-3234
R.R. 2
Chase, B.C. V0E 1N0

Logging Locations

Adams Lake
Bear Bay
Bear Lake
Bute
Chamiss
Cleagh Creek
Drury Inlet
Grilse Creek
Helilog Eclipse
Hope (3)
Kingcome Inlet
Kumealon
Kwatna
Malcolm Island
Narrows Inlet
Pemberton
Porcher
Port Neville
Scott Cove
Seymour Inlet
Taleomey
Tsuadhi Creek
Whonnock (3)

Photo credit: coastal scene, Ministry of Forests.

LITHO'D IN CANADA
AGENCY PRESS