

An aerial photograph of a vast lumber yard. The yard is filled with numerous long, rectangular stacks of cut lumber, arranged in a grid-like pattern. The wood has a warm, golden-brown hue. In the bottom left corner, a small boat with a white and red hull is moving through the dark water, leaving a white wake. The overall scene is captured from a high angle, looking down on the stacks.

DOMAN INDUSTRIES LIMITED

ANNUAL REPORT 1981

DOMAN INDUSTRIES LIMITED

(Incorporated under the laws of British Columbia)

Board of Directors

- H. S. Doman, President and Chairman of the Board, Doman Industries, Duncan, B.C.
- I. C. Danvers, Executive, Phoenix, Arizona.
- J. C. Davie, Barrister & Solicitor, Williams, Davie & Company, Duncan, B.C.
- J. R. Abercrombie, C.A., Vice President, Doman Industries, Duncan, B.C.
- J. R. Frumento, Vice President, Doman Industries, Duncan, B.C.
- F. D. Radler, Vancouver, B.C., President, Sterling Newspapers Ltd. and Dominion Malting Limited and Vice President, Argus Corporation Limited.

Audit Committee

- F. D. Radler, Chairman
- I. C. Danvers
- J. R. Abercrombie

Officers

- H. S. Doman, President
- J. C. Davie, Secretary
- J. R. Abercrombie, Treasurer, Vice President Finance and Administration
- J. R. Frumento, Vice President Timber and Manufacturing

Head Office

435 Trunk Road
Duncan, B.C.
V9L 2P8
(tel. 604-748-3711)

Transfer Agent and Registrar for Common Shares

Royal Trust Company, Vancouver, B.C. and Toronto, Ontario

Stock Exchanges

Common Shares — Toronto and Vancouver

Transfer Agent and Registrar for 10¼% Series A Debentures

The Canada Trust Company
Montreal, Toronto, Winnipeg,
Calgary and Vancouver

Bankers

The Royal Bank of Canada

Solicitors

Williams, Davie & Company, Duncan, B.C.

Auditors

Thorne Riddell, Vancouver, B.C.

Annual Meeting

The Annual General Meeting of the Shareholders of the Company will be held in Duncan, B.C. at the Village Green Inn on Tuesday April 27, 1982 at 2:00 p.m.

Financial Highlights

For the years ended December 31,

(thousands of dollars)

	1981	1980	1979	1978
Sales.....	115,793	110,565	113,178	115,302
Earnings (loss) after taxes.....	(10,902)	1,847	10,680	11,081
Cash flow (negative) from operations	(7,694)	7,655	16,983	14,254
			(dollars)	
Earnings (loss) per share	(1.65)	.28	1.62	1.68
Cash flow (negative) per share.....	(1.17)	1.16	2.57	2.16
Dividends paid per share35	.40	.25	.47
Price range (TSE) — high	13.00	12.25	9.50	9.50
— low	4.05	6.375	6.00	4.70
— close	7.00	11.625	7.00	7.125

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President's Report to the Shareholders

The Company and its Industry

The principal business of Doman Industries is the manufacture of lumber on the coast of British Columbia. Most of this lumber is exported. This is a cyclical business subject to wide fluctuations in supply and demand. Business volumes and profit levels are influenced by economic conditions in our main market areas, which in 1981 in order of importance were the United States, Canada, and Offshore. Competition for business in these markets comes mainly from lumber producers in the United States, Eastern Canada, the U.S.S.R., Finland and Sweden. The competitive position of Canadian lumber mills in relation to those in other countries is influenced by the availability of raw material, the value of the Canadian dollar, and our experience in relation to theirs in respect to inflation, interest costs, energy costs, plant efficiency, labour costs and productivity. In general, the competitive position of Canadian producers is good. The competitive position of Doman Industries in respect to other Canadian producers is strong. The Company currently operates three modern and efficient sawmills each of which enjoys a high productivity rate. These three mills represent over 80% of our lumber production capacity. Two smaller sawmills represent the remaining 20% of our lumber production capacity.

We are in a cyclical business as the events of 1981 and 1980 have clearly shown. We do not prosper in a recession. We are however among the first to benefit when conditions improve, because a recovery in the North American housebuilding industry on which we depend usually leads the way out of each recession.

Western Forest Products Limited

Doman Industries owns one third of Western Forest Products Limited, (Western). This is a major investment in a company which not only is subject to the wide cyclical swings of the Forest Industry, but in 1981 also required major corrective measures to get its operations trimmed down and manageable. When we went into this venture in October 1980 the assets included five



sawmills, two pulp mills, three tree farms, several forms of tenure in public sustained yield units, old temporary timber tenures and fee simple lands. In 1981 Western sold its Alberta sawmill and certain other properties, closed one sawmill permanently, and in December leased its remaining three sawmills, one to each of its three shareholders. Doman Industries took over the New Westminster sawmill from Western on December 1, 1981 on a five year lease with option to purchase. These steps took time. Staff severance payments were expensive, and disruptions during this period of change in Western were costly. However, this trimming has been done, and Western is now a pulp and timber company operating its two pulp mills and its logging operations all on the B.C. coast.

1981 Operating Results

In 1981 our sales were \$115,793,000 up 5% from 1980 sales of \$110,565,000. In 1981 the Company lost \$2,771,000 or 42 cents per share before accounting for its investment in Western Forest Products Limited. The Company's cost in 1981 of carrying the Western investment including our equity in the losses of Western and interest expensed in respect to the cost of our investment, net of tax, amounted to \$8,131,000 or \$1.23 per share, bringing the Doman Industries net loss for the year to \$10,902,000 or \$1.65 per share. In 1980 our net profit was \$1,847,000 or 28 cents per share. I am sorry to have to report this huge loss for 1981.

Doman Industries and Western were hit hard in 1981 by severely depressed lumber and log markets, and by extremely high interest rates. The cure for inflation in the United States resulted in a virtual collapse of the housebuilding industry in that country in 1981 and one by one other world markets for lumber lost their strength as North America's economic problems spread world wide.

During this period we curtailed our sawmill and logging operations, and cut back on all costs and capital expenditures which were not absolutely essential. These measures will continue until our markets return. A similar program has been followed by Western and that company has been cut back to a pulp and timber operation. In Doman Industries the Directors have decided to omit the payment of the dividend for the first quarter of 1982, the only interruption of our regular quarterly dividend since dividend number one was paid in January 1972. These are drastic steps, but we are living in very uncertain times which call for extreme measures.

Labour

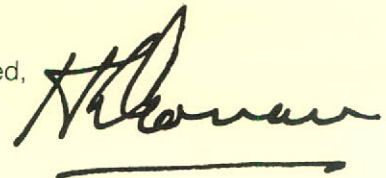
1981 was a contract negotiation year for the B.C. forest industry. During these negotiations labour stoppages resulted in the loss of two months production and in delayed lumber shipments. In 1981 the Company paid salaries, wages and employment benefits of \$21,000,000 (1980 \$20,400,000). The Company currently employs 780 people on a full time basis, down from 865 people at this time last year. A significant increase in the number of employees took place in 1981 when we acquired the New Westminster sawmill and when the second shift started at the new Nanaimo sawmill. All other divisions of the Company in every area of its endeavours have experienced reductions in the numbers employed in 1981. Employment will approximate 1,010 full time people when economic conditions improve and we can operate at full production.

Outlook

We may be in for another six months of difficult business conditions. Interest rates, consumer confidence and the world wide economic climate are all beyond our control. However, we can control the efficiency of our business. We have trimmed back everywhere, and in response to market conditions our sawmills are operating two shifts rather than three shifts daily on a five day week basis except for Ladysmith which is on a 3 shift basis and Chemainus which is on a 1 shift basis. We are in a holding pattern awaiting the next cyclical upturn in housebuilding and lumber demand. This time Doman Industries has 580 million board feet of annual lumber production capacity compared with the 300 million board feet we had available in the 1978-79 boom period. We have valuable assets, not the least of which is an experienced and efficient work force. Most of our physical plant is at the forefront of modern technology and could not be replaced at anywhere near the cost shown on the balance sheet. Our timber position could probably not be replaced and even if available, could not be replaced at an economically feasible cost. We are fortunate to have extensive logging development and these modern lumber production facilities built and in place.

The timing of the U.S. recovery and the spill over effect on the world economic scene and on Canadian economic activity and interest rates is critical to our industry. Increased housebuilding activity is the first indicator that a recession is over as housebuilding traditionally leads the way in an economic recovery. Your Company has suffered greatly during this recession and will be among the first to benefit when economic conditions improve.

Respectfully submitted,



H. S. Doman
President and Chairman of the Board

DUNCAN, B.C. March, 1982.

About the Company

The business of Doman Industries Limited includes logging, sawmilling, lumber remanufacturing, truck transportation, domestic marketing of building supplies and export marketing of lumber. The Company is vertically integrated in the lumber industry.

Sales according to the main categories of business over the past five years have been:

	1981	1980	1979	1978	1977
	(in millions of dollars)				
Logging, manufacturing and exporting	87	83	90	94	70
Domestic building supplies	20	19	15	14	15
Truck transportation	9	9	8	7	7
Total	<u>116</u>	<u>111</u>	<u>113</u>	<u>115</u>	<u>92</u>

LOGGING

Doman Industries operates four major logging divisions on the coast of British Columbia located at Jervis Inlet, Nootka Island, Rivers Inlet and Kimsquit River. These four divisions operate on Public Sustained Yields Units ("PSYU's") which are areas of Crown land managed by the Forest Service of British Columbia. Typically, a PSYU provides the timber needs of a number of operators each holding a form of tenure. The Forest Service calculates the rate of annual timber cutting which will permit the area to provide a sustained yield over time. Doman Industries' logging operations at the above four locations are based on tenures known as Timber Sale Harvesting Licences ("TSHL's"). Under this form of tenure, Doman Industries has the right to harvest a specified amount of timber, known as its allowable annual cut, and has some responsibilities for reforestation and fire protection. Authority to cut is conferred by the Forest Service through the issuance, as required, of cutting permits. The Company also has several small logging operations based on Timber Sale Licences which permit the Company to cut Crown timber on a designated tract of land within a PSYU.

LOG SUPPLY

The Company is able to supply two-thirds of the logs required for the 580 million board feet annual rated capacity of its five sawmills from Doman logging divisions, logs contractually committed to Doman and logs acquired on a fibre exchange basis for Doman sawmill by-products. The remaining one-third of the logs required are obtained on the Vancouver log market and from independent suppliers on Vancouver Island.

SAWMILLS

Doman Industries owns and operates four sawmills, and from December 1, 1981 has leased with a five year option to purchase, the New Westminster sawmill of Western Forest Products Limited. These sawmills are situated close to the deep sea docks and the rail lines over which their lumber is shipped. Three of the sawmills are located on tidewater at Nanaimo, Ladysmith and Cowichan Bay on Vancouver Island. The fourth is a dryland sawmill at Chemainus on Vancouver Island. The New Westminster sawmill is located on the Fraser River.

The Nanaimo plant includes a large log sawmill and a lumber remanufacturing plant. This sawmill has an annual lumber production capacity of 200 million board feet and the design allows for significant expansion. The remanufacturing plant is an integral part of the Nanaimo sawmill and provides the facilities to upgrade lumber without slowing down the sawmill's production flow. The Nanaimo remanufacturing plant is also able to process lumber and cants from other sawmills. An important feature of the Nanaimo plant is a barge load-out to handle waterborne shipments of by-products from the Company's Vancouver Island sawmills. The Cowichan Bay sawmill cuts small and medium sized logs and has an annual lumber production capacity of 145 million board feet. The Ladysmith sawmill cuts predominantly small logs and has an annual lumber production capacity of 125 million board feet. The mill at Chemainus has an annual lumber production capacity of 30 million board feet and cuts all sizes of logs. The adjacent

remanufacturing plant handles both lumber from this sawmill and lumber purchased from others. The New Westminster sawmill has an annual lumber production capacity of 80 million board feet. All five sawmills have planer mills attached which are part of the manufacturing process.

Sawmill by-products include pulp chips, sawdust and hog fuel. Most of the Company's Vancouver Island sawmill by-products are moved by truck to two Vancouver Island pulp mills and the balance is shipped by barge from facilities at the Nanaimo sawmill. By-products of the New Westminster sawmill are shipped by barge from facilities at that mill.

LUMBER PRODUCTION

The combined lumber production capacity of the five sawmills of Doman Industries, on a three shift five day week basis, is now 580 million board feet, (mfbm), annually, 1981 500 mfbm, 1980 300 mfbm. Actual lumber production in 1981 was reduced by the two month B.C. coast lumber strike. In both 1981 and 1980 lumber production was curtailed because of poor market conditions.

Lumber production over the past five years (including production of a small Vancouver mill sold in 1978) has been:

	Year ended December 31				
	1981	1980	1979	1978	1977
Lumber production	245	248	240	305	343

LUMBER MARKETING

Doman's lumber is sold through its five domestic building supply outlets on Vancouver Island and in the Vancouver area. Other Canadian markets are serviced by truck and by rail. U.S. markets are serviced by truck, rail, barge and ship. Deliveries to offshore markets are by ship. Doman Industries owns a 47% interest in Eacom

Timber Sales Limited, the third largest ocean cargo shipper of lumber in Canada, and conducts a portion of its export lumber sales through Eacom. Canadian truck and rail shipments together with lumber sales from the five building supply outlets accounted for 17% of lumber footage sold in both 1981 and 1980. Barge shipments to points in California together with U.S. rail business represented 24% of lumber footage sold in 1981 and 25% in 1980. Sales on the U.S. east coast, where our lumber is delivered by ship accounted for 51% of 1981 lumber footage sold, up significantly from 25% in 1980. Offshore markets accounted for 8% of 1981 Doman lumber footage sold, down from 33% in 1980.

The distribution of lumber footage sold over the past five years has been:

	1981	1980	1979	1978	1977
Canada	17%	17%	14%	12%	13%
United States.....	75	50	61	79	80
Other Export	8	33	25	9	7
	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

TRANSPORTATION

The Transportation division of the Company conducts a public freight business in British Columbia, Washington and Oregon. This division owns 77 highway diesel tractors and 177 trailers. Additional equipment is leased as required to meet the demand in peak periods. The business of this division is handling trailer load lots principally for the forest industry and the construction industry. Specialized pieces of equipment for hauling pulp chips, hog fuel, sawdust, chemicals and other bulk cargoes are operated by this division. This specialized hauling is an important part of our business. In addition to its public freight business the transportation division does the hauling for the Doman sawmills on Vancouver Island and for the Doman Building Supply Centres in British Columbia. Truck dispatch and repair facilities are located at Duncan on Vancouver Island and at Richmond, B.C. Annual sales of this division in 1981 were \$9 million.

DOMESTIC MARKETING OF BUILDING SUPPLIES

The Company's domestic building supply yards are all located in British Columbia, with two in Victoria and one in each of Duncan, Nanaimo and Surrey. The Duncan yard is complemented by Armour & Saunders Ltd., a wholly-owned subsidiary of the Company, which operates a ready-mix concrete business. The five building supply yards are supported by bulk assembly yards at Chemainus on Vancouver Island and at Richmond, B.C. The domestic division sells lumber and a full range of building materials. Annual sales of this division in 1981 were \$20 million.

WESTERN FOREST PRODUCTS LIMITED

Doman Industries owns one-third of the shares of Western Forest Products Limited, (Western). The other shareholders of Western are British Columbia Forest Products Limited and Whonnock Industries Limited each of which owns one-third of the shares. On October 30, 1980 Western purchased the British Columbia and Alberta assets of the Rayonier Canada Division of ITT Industries of Canada Ltd., (Rayonier), a wholly-owned subsidiary of International Telephone & Telegraph Corporation. In a separate transaction, Western acquired the remaining 40% interest in Western Forest Industries Ltd., (WFI), a Rayonier subsidiary. Each of the shareholders contributed \$60 million to the share capital of Western. The balance of the funds required for the purchase price and for Western's capital improvement program have been borrowed by Western. Doman Industries has not guaranteed any of Western's debt.

In 1981 Western sold its Alberta sawmill and certain other properties not required in its coastal B.C. operations. The WFI sawmill on Vancouver Island was closed permanently in 1981, and on December 1, 1981 the three remaining sawmills of Western were leased to its shareholders for five years with an option to purchase. Doman Industries began operating the New Westminster sawmill on this basis on December 1, 1981.

Western is now a pulp and timber company operating a kraft pulp mill at Woodfibre on Howe Sound, B.C., and a sulphite dissolving pulp mill at Port Alice on Vancouver Island, three Tree Farm Licenses (TFL's), fee simple lands some of which are under sustained yield management and certain old temporary timber tenures on the coast of British Columbia. WFI owns 34 thousand acres of fee simple land on Vancouver Island. Western is an important supplier of logs to Doman Industries.

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Financial Summary 1971-1981

(thousands of dollars except for earnings per share which are in dollars)

Beginning with 1976 figures are for the twelve months ended December 31, prior to 1976 figures are for the twelve months ended October 31.

	1981	1980	1979	1978
Earnings				
Sales.....	115,793	110,565	113,178	115,302
Earnings (loss) before income taxes.....	(16,991)	1,861	18,085	19,565
Income taxes.....	(6,089)	14	7,405	8,484
Net earnings (loss)	(10,902)	1,847	10,680	11,081
Earnings (loss) per common share	(1.65)	.28	1.62	1.68
Cash Flow				
Operations (negative)	(7,694)	7,655	16,983	14,254
Issue of long-term debt	15,000	80,000	—	—
Sale of fixed assets	1,020	472	125	1,543
Purchase of fixed assets	7,304	28,386	18,944	5,884
Reduction of long-term debt.....	591	235	738	433
Sundry use (source) of funds	1,111	(965)	64	1,000
Dividends.....	1,980	2,641	2,146	3,495
Investment Western Forest Products	5,910	61,471	—	—
Increase (decrease) in working capital..	(8,570)	(3,641)	(4,784)	4,985
Balance Sheet				
Current assets.....	56,209	60,678	46,253	44,090
Current liabilities.....	47,855	43,754	25,688	18,741
Working capital.....	8,354	16,924	20,565	25,349
Fixed assets — net.....	63,507	61,541	37,631	22,413
Other assets	65,703	64,314	5,199	5,159
Long-term indebtedness.....	114,115	99,706	19,942	20,680
Deferred income taxes	697	7,439	7,025	4,347
Shareholders' equity	22,752	35,634	36,428	27,894
Interest of minority shareholders	—	—	—	—

1977	1976	1975	1974	1973	1972	1971
92,022	68,956	34,648	38,843	42,483	26,330	20,816
10,941	4,772	2,825	4,118	9,409	4,674	3,043
4,977	1,895	1,492	2,116	4,723	2,406	1,682
5,964	2,877	1,333	2,002	4,686	2,268	1,361
.90	.44	.20	.30	.72	.35	.21
8,479	5,560	3,174	3,294	6,453	3,386	2,313
20,000	1,039	7,820	122	2,031	598	1,158
271	425	185	162	143	256	47
2,799	2,520	8,153	1,918	4,033	2,303	1,350
9,898	1,001	1,101	432	249	129	273
1,819	1,947	543	502	47	359	402
660	655	652	1,361	560	181	39
—	—	—	—	—	—	—
13,574	901	730	(635)	3,738	1,268	1,454
40,063	29,741	19,617	13,852	18,571	9,812	6,736
19,699	22,951	11,459	6,424	10,508	5,487	3,679
20,364	6,790	8,158	7,428	8,063	4,325	3,057
20,084	19,707	17,579	10,662	9,877	6,866	5,422
4,134	2,603	1,361	1,087	1,231	964	657
21,112	11,010	11,178	4,463	4,806	3,115	2,749
3,162	3,082	1,617	1,133	1,103	766	664
20,308	15,008	13,034	12,349	11,676	7,459	5,267
—	—	1,269	1,232	1,586	815	456

Consolidated Statement of Earnings and Retained Earnings

(thousands of dollars except for earnings per share which are in dollars)

For the years ended December 31,	1981	1980
Sales of products, merchandise and services.....	<u>115,793</u>	<u>110,565</u>
Costs and expenses		
Cost of sales	101,363	92,837
Selling and administration.....	5,375	5,102
Depreciation	2,474	2,356
Depletion of timber and amortization of roads	1,915	1,992
Amortization of preproduction costs	161	242
Interest, excluding interest on Western Forest Products Limited investment	<u>8,999</u>	<u>5,472</u>
	<u>120,287</u>	<u>108,001</u>
Earnings (loss) from operations	(4,494)	2,564
Equity in losses of joint venture companies, excluding Western Forest Products Limited.....	<u>583</u>	<u>703</u>
Earnings (loss) before income taxes and before accounting for investment in Western Forest Products Limited	<u>(5,077)</u>	<u>1,861</u>
Income taxes		
Current	653	(400)
Deferred.....	<u>(2,959)</u>	<u>414</u>
	<u>(2,306)</u>	<u>14</u>
Earnings (loss) before accounting for investment in Western Forest Products Limited.....	<u>(2,771)</u>	<u>1,847</u>
Per share	<u>(.42)</u>	<u>.28</u>
Western Forest Products Limited		
Interest expense	7,370	—
Less deferred income taxes	<u>3,783</u>	<u>—</u>
Interest expense net of deferred income taxes	3,587	—
Equity in losses of Western Forest Products Limited.....	<u>4,544</u>	<u>—</u>
Western Forest Products Limited effect on earnings (losses) of Doman Industries Limited	<u>(8,131)</u>	<u>—</u>
Per share	<u>(1.23)</u>	<u>—</u>
NET EARNINGS (LOSS) FOR THE YEAR	<u>(10,902)</u>	<u>1,847</u>
Per share	<u>(1.65)</u>	<u>.28</u>
RETAINED EARNINGS AT BEGINNING OF YEAR	33,793	34,587
Net earnings (loss) for the year	<u>(10,902)</u>	<u>1,847</u>
	22,891	36,434
Deduct		
Dividends	<u>1,980</u>	<u>2,641</u>
RETAINED EARNINGS AT END OF YEAR	<u>20,911</u>	<u>33,793</u>

Consolidated Statement of Changes in Financial Position

(thousands of dollars)

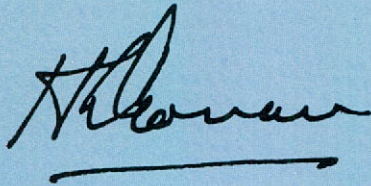
For the years ended December 31,	1981	1980
WORKING CAPITAL DERIVED FROM		
Operations.....	—	7,655
Increase in long-term debt	15,000	80,000
Disposal of fixed assets, net of gains and losses	<u>1,020</u>	<u>472</u>
	<u>16,020</u>	<u>88,127</u>
WORKING CAPITAL APPLIED TO		
Operations.....	7,694	—
Additions to fixed assets	7,304	28,386
Reduction of long-term debt.....	591	235
Increase in investments.....	7,021	60,506
Dividends	<u>1,980</u>	<u>2,641</u>
	<u>24,590</u>	<u>91,768</u>
DECREASE IN WORKING CAPITAL	8,570	3,641
Working capital beginning of the year.....	<u>16,924</u>	<u>20,565</u>
WORKING CAPITAL END OF THE YEAR	<u>8,354</u>	<u>16,924</u>

Consolidated Balance Sheet

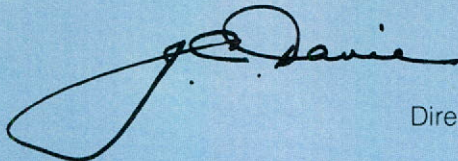
(thousands of dollars)

	Assets	
As at December 31,	1981	1980
CURRENT ASSETS		
Cash.....	378	44
Accounts receivable	13,995	12,389
Inventories (note 2)	40,573	43,841
Prepaid expenses	<u>1,263</u>	<u>4,404</u>
	<u>56,209</u>	<u>60,678</u>
 INVESTMENTS (note 3).....	 <u>65,091</u>	 <u>63,367</u>
 FIXED ASSETS		
Land, buildings, machinery and equipment (note 4)	65,882	61,795
Less accumulated depreciation	<u>13,498</u>	<u>11,371</u>
	52,384	50,424
 Timber holdings and logging roads, less amounts written off	 <u>11,123</u>	 <u>11,117</u>
	<u>63,507</u>	<u>61,541</u>
 DEFERRED COSTS, less amortization	 <u>612</u>	 <u>947</u>
	<u>185,419</u>	<u>186,533</u>

On Behalf of the Board:



Director



Director

Liabilities

As at December 31,	1981	1980
CURRENT LIABILITIES		
Bank indebtedness (note 5)	31,457	31,379
Accounts payable and accrued liabilities	16,380	12,358
Principal due within one year on long-term debt	18	17
	<u>47,855</u>	<u>43,754</u>
 LONG-TERM DEBT (note 5)	 114,115	 <u>99,706</u>
 DEFERRED INCOME TAXES	 697	 <u>7,439</u>

Shareholders' Equity

SHARE CAPITAL (note 6)		
Authorized 5,000,000 Class A Preferred Shares without par value		
13,363,184 common shares without par value		
Issued 6,601,680 common shares	1,841	1,841
 RETAINED EARNINGS	 20,911	 33,793
	<u>22,752</u>	<u>35,634</u>
	<u>185,419</u>	<u>186,533</u>

Auditors' Report

To the Shareholders of
Doman Industries Limited

We have examined the consolidated balance sheet of Doman Industries Limited as at December 31, 1981 and the consolidated statements of earnings and 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, 1981 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 on a basis consistent with that of the preceding year.

Vancouver, Canada
February 5, 1982

Thorne Riddell
Chartered Accountants

Notes to Consolidated Financial Statements

Year ended December 31, 1981.

1. ACCOUNTING POLICIES

(a) Basis of Consolidation

The consolidated financial statements include the accounts of the Company and all of its subsidiaries.

(b) Inventories

Inventories are valued at the lower of cost and net realizable value.

(c) Investments

Investments in joint venture companies are recorded on the equity basis and therefore the values at which they are carried on the balance sheet are adjusted by the Company's share in their undistributed earnings or losses.

Western Forest Products Limited (Western), one third owned, has deferred all expenses including interest on borrowings for the original acquisition of assets, net of revenues, for an initial six months period of planning and orientation which ended April 30, 1981. These deferrals by Western totalled \$20,774,000 to that date, and are being amortized against the earnings of Western over the five year period commencing November 1, 1981.

From May 1, 1981 Western has deferred interest charges on initial borrowings identified with its Squamish pulp mill, Woodfibre, which is being rebuilt, and with the timber relating to this mill, less the operating profits net of losses of Woodfibre to the end of the reconstruction period. These deferred charges amounted to \$11,558,000 to October 31, 1981 and will be amortized against the earnings of Western upon the completion of the rebuild.

The investment of the Company in Western has been increased by the interest for the six months ended April 30, 1981 on the \$60 million borrowed for the acquisition. This deferred interest amounted to \$1,471,000 in 1980 and \$3,558,000 in 1981, a total of \$5,029,000 and is being written off and charged against the earnings of the Company over the five year period which commenced November 1, 1981. The amount amortized and written off against earnings in 1981 was \$170,000.

From May 1, 1981 the Company has added to the cost of its investment \$2,352,000 being the proportion of interest on monies borrowed to make the investment which is the same proportion of interest charges being deferred from May 1, 1981 by Western in respect to its initial borrowings identified with Woodfibre. These charges will be amortized against earnings on the completion of the Woodfibre rebuild.

Other investments are recorded at cost.

(d) Fixed Assets

Fixed assets are stated at cost including interest during construction of major projects. Depreciation is provided on a straight-line basis for the period of operations at rates based on the estimated useful lives of the assets. The estimated useful lives range between five to ten years for automotive equipment, ten to fifteen years for other equipment and twenty to twenty-five years for buildings. Costs of timber holdings and logging roads are written off as timber is removed.

(e) Deferred Costs

Deferred costs consist of expenses related to the debenture issue which are being amortized over ten years.

(f) Income Taxes

The Company charges earnings with income taxes related to these earnings. Any difference between these taxes and the taxes currently payable are shown as deferred income taxes.

2. INVENTORIES

(thousands of dollars)

	1981	1980
Logs	18,106	24,034
Lumber.....	18,695	16,175
Merchandise	2,401	2,363
Supplies.....	1,371	1,269
	<u>40,573</u>	<u>43,841</u>

3. INVESTMENTS

(thousands of dollars)

	1981	1980
Western Forest Products Limited.....	62,667	61,471
Other joint venture companies.....	212	701
Other investments	2,212	1,195
	<u>65,091</u>	<u>63,367</u>

Condensed consolidated financial information for Western Forest Products Limited at its year end October 31, 1981 is as follows:

WESTERN FOREST PRODUCTS LIMITED

Balance Sheet — October 31, 1981

(thousands of dollars)

ASSETS

Current assets.....	121,036
Fixed assets	403,803
Deferred expenses	32,332
Other assets, net	964
	<u>558,135</u>

CURRENT LIABILITIES

Accounts payable and operating loans.....	110,969
Term bank loans, reclassified as current	280,797
	<u>391,766</u>

SHAREHOLDERS' EQUITY

Share capital	180,000
Deficit	(13,631)
	<u>166,369</u>
	<u>558,135</u>

Western Forest Products term bank loans of \$280,797,000 are reflected as current liabilities because Western has not satisfied

certain covenants under its bank loan agreement. Doman Industries has not guaranteed any of the Western Forest Products debt.

For the year ended October 31, 1981 the sales of Western were \$260,628,000 and the loss was \$13,631,000 of which one third or \$4,544,000 has been booked as an equity loss by Doman Industries Limited. On the same basis Western's loss for November and December 1981 applicable to Doman Industries was \$1,150,000 and will be included in the 1982 operating results of the Company.

4. FIXED ASSETS

(thousands of dollars)	1981	1980
Land	2,961	2,460
Buildings	16,935	15,338
Machinery and equipment	45,986	43,997
	65,882	61,795
Accumulated depreciation	13,498	11,371
	<u>52,384</u>	<u>50,424</u>

5. LONG-TERM DEBT

(thousands of dollars)	1981	1980
Loans secured by first mortgages:		
Sinking fund debentures Series A, 10¼% due December 1997, retractible at the option of the holder on December 15, 1987 ..	18,491	19,063
Royal Bank capital loan due 1983	15,000	—
Royal Bank capital loan due 1995	20,000	20,000
Royal Bank capital loan due 1994	60,000	60,000
Other	642	660
	114,133	99,723
Principal included in current liabilities	18	17
	<u>114,115</u>	<u>99,706</u>

The sinking fund debentures are secured by fixed and floating charges on certain assets of the Company and certain of its subsidiary companies. The trust agreement relating to the debentures requires the Company to establish sinking funds to retire in each of the years 1988 to 1996 5% of the principal balance of the debentures outstanding on December 15, 1987.

The Royal Bank capital loans for \$20,000,000 and \$60,000,000 bear interest at the bank prime rate plus ½%. The capital loan for \$15,000,000 bears interest at the bank prime rate plus ¾%. At the Company's option these rates may be fixed for varying periods at rates based on the bank's U.S. base rate, Eurodollar rates or Banker's Acceptances.

The Royal Bank capital loan for \$60,000,000 due 1994 is secured by the shares owned by the Company in Western Forest Products Limited. These capital loans together with current bank indebtedness are also secured by assignment of accounts receivable and inventories and by a \$25,000,000 second floating charge debenture.

Long-term debt maturing in the next five years is as follows:

(thousands of dollars)			
1982	18	1985	2,000
1983	15,000	1986	2,000
1984	2,000		

6. SHARE CAPITAL

The authorized share capital was increased during the year by the authorization of 5,000,000 Class A preferred shares. None has been issued.

Outstanding options granted to directors and officers of the Company to purchase a total of 60,000 common shares at \$7.76 per share may be exercised up to 1990.

7. OTHER INFORMATION

(a) RELATED PARTY TRANSACTIONS

Included in total sales for the period are sales of \$29,933,000 (1980 \$22,467,000) made to a joint venture company. Accounts receivable included \$1,239,000 (1980 — \$1,796,000) due from the joint venture company.

(b) EXPORT SALES

The company's export sales by geographic area were as follows:

(thousands of dollars)	1981	1980
United States.....	40,984	24,567
Europe	3,832	12,314
Other.....	2,541	10,989
	<u>47,357</u>	<u>47,870</u>

(c) Remuneration of directors and senior officers was \$559,000.

Five Year Operating Results by Quarter

(thousands of dollars except for earnings per share which are in dollars)

For the years ended December 31,	1981	1980	1979	1978	1977
SALES					
First quarter	30,859	28,680	23,146	21,978	20,993
Second quarter	34,755	26,893	26,817	28,807	20,779
Third quarter	24,658	29,886	35,757	32,889	28,597
Fourth quarter	25,521	25,106	27,458	31,628	21,653
Year	115,793	110,565	113,178	115,302	92,022
NET EARNINGS					
First quarter	(713)	1,278	2,548	1,468	1,092
Second quarter	231	(329)	2,387	2,451	1,064
Third quarter	(3,527)	339	3,716	3,271	2,563
Fourth quarter	(6,893)	559	2,029	3,891	1,245
Year	(10,902)	1,847	10,680	11,081	5,964
EARNINGS PER SHARE					
First quarter	(.11)	.19	.39	.22	.17
Second quarter04	(.05)	.36	.37	.16
Third quarter	(.54)	.06	.56	.50	.38
Fourth quarter	(1.04)	.08	.31	.59	.19
Year	(1.65)	.28	1.62	1.68	.90
CASH FLOW					
First quarter	29	2,669	3,406	723	1,281
Second quarter	(28)	181	3,048	3,232	1,464
Third quarter	(3,907)	2,369	6,123	4,429	3,613
Fourth quarter	(3,788)	2,436	4,406	5,870	2,121
Year	(7,694)	7,655	16,983	14,254	8,479

History of Doman Industries

Founded in 1955, Doman Industries began by operating the business of Mr. H. S. Doman, who commenced his career as a sole proprietor hauling lumber and copper ore under contract, selling lumber to building supply contractors and selling sawdust and wood fuel on Vancouver Island. In the ten year period to 1964 the business was expanded to include retail and wholesale merchandising of lumber and building supplies, contract freight hauling, logging, sawmilling and lumber remanufacturing. In 1964 Doman Industries became a public company and in 1965 its shares were listed on the Vancouver Stock Exchange. In 1965 a ready-mix concrete business was acquired.

The first major sawmill was built at Ladysmith in 1966. In 1969 the Company acquired its first Timber Sale Harvesting Licence. There was a 3 for 1 common share stock split in 1969 and these shares were called for trading on the Toronto Stock Exchange in 1970. Common share dividends commenced in 1972 and the shares were split 2 for 1 in 1973. A small sawmill was built at Chemainus in 1973 on the site of a mill destroyed by fire in the preceding year. The Company's second major

sawmill was constructed at Cowichan Bay in 1975. In 1976 the common shares were split a third time, this time 2 for 1. In 1977 the Company was awarded three Timber Sale Harvesting Licences to support a new sawmill at Nanaimo and to support a pulpmill development planned for the 1980's. In the period 1978 through 1980 logging operations were developed. In 1979 and 1980 the Company's largest sawmill was constructed at Nanaimo. This mill started operations in December 1980.

On October 30, 1980 Doman Industries acquired a one-third interest in Western Forest Products Limited, a major integrated forest products company.

The events of 1981 are covered elsewhere in this report.

