Great Lakes Forest Products Limited Annual Report 1983

OUR COMPANY

Great Lakes Forest Products Limited, incorporated under the laws of Ontario in 1936, acquired the assets of a predecessor company which went into receivership in the early 1930's. These assets, located on the company's present mill site in Thunder Bay, included two newsprint machines. During the late 1930's and 1940's, the new company improved and modernized its facilities, acquired additional licensed forest lands and established itself in the U.S. newsprint market. In the mid-1950's extensive expansion took place with the addition of Nos. 3 and 4 newsprint machines. The expansion included enlargement of such operations as groundwood pulp production, wood handling and timber harvesting.

Over the years the company's woodlands operations evolved from the horse-drawn methods of old to modern mechanized systems. A leader in woodlands mechanization, the company continues to play an important role in the development of improved operating methods.

In 1966 the first kraft pulp mill went into operation providing diversification and permitting more complete use of tree species in the company's forest areas.

Further diversification and expansion took place during the 1970's with the construction and subsequent expansion of a stud lumber mill, construction of a waferboard plant and the addition of the second kraft pulp mill.

With the construction of the first kraft pulp mill, the company commenced a comprehensive environmental control program and has gained widespread recognition over the years for leadership in this field.

In 1979 the Dryden, Ontario assets of Reed Ltd. were acquired and since 1980 the company has undertaken extensive modernization and expansion of the Dryden kraft pulp mill and fine paper mill, as well as construction of a stud lumber mill. The kraft pulp and stud lumber mills commenced operation in 1983 and the fine paper machine is scheduled for completion in March 1984.

The company manufactures the following products: *bleached kraft pulp*, a prime ingredient in a wide range of paper products from high quality printing papers to disposable paper products for home and medical use; *newsprint*, the paper on which newspapers are printed; *fine papers*, printing papers, similar to the papers used for the cover and the financial section of this report, copy papers and paper that is converted to envelopes of varying sizes and styles to meet commercial and personal mailing needs; *stud lumber*, precision cut 2 × 4's for use in housing and light construction and *waferboard*, a tough, water-resistant building board for exterior sheathing, interior panelling, roofing and floor underlayment.

Pulp is sold through Lake Superior Pulp and Paper Inc., White Plains, N.Y.; R. L. Nash is president and F. M. Jennings, vice-president. Servicing of our newsprint contracts is handled by Lake Superior Newsprint Co., Chicago; W. D. Frost is president and O. E. Babcock, vice-president. Fine papers are marketed through the company's offices in Toronto and Winnipeg; John H. Sim is director, fine paper sales. Stud lumber and waferboard are marketed by St. Regis Corporation; James D. Kingston is director, building products sales.

Common share transfer agents and registrars are The Royal Trust Company, Toronto, Montreal and Calgary and the Bank of Montreal Trust Company in New York.

Great Lakes Forest Products Limited head office and mailing address is P.O. Box 430, Thunder Bay, Ontario, P7C 4W3.

Price Range of our Common Stock

Year	High	Low
1979	$53.00	$40.50
1980	73.50	44.00
1981	93.50	67.00
1982	81.50	46.00
1983	91.50	58.50

Our Net Earnings and Dividends

Year	Net Earnings (Loss)	Dividends Declared
	per share	
1979	$12.44	$1.50
1980	18.01	2.00
1981	16.59	2.90
1982	3.80	3.20
1983	(2.03)	1.20

Cover paper is vellum offset made in our Dryden fine paper mill.

HIGHLIGHTS

'000 omitted	1983	1982
Net sales: Pulp and paper	$453,185	$416,246
Building products	41,796	21,608
Total	494,981	437,854
Operating profit	35,429	57,203
Earnings (loss) before income taxes	(22,901)	17,350
Income taxes	(12,965)	(1,202)
NET EARNINGS (LOSS): Total amount	(9,936)	18,552
Per share	(2.03)	3.80
Cash flow	16,416	71,622
Expenditures on fixed assets	56,023	168,765
Working capital at year end	26,695	48,991

Five-year shipment and financial summaries are shown on pages 19, 22 and 23.

- ☐ High worldwide inventories and intense competition led to lower average prices for our major products resulting in a loss of $9.9 million or $2.03 per share versus net earnings of $18.6 million or $3.80 per share in 1982.
- ☐ Despite the pressure on prices, net sales of $495 million were higher than $437.9 million in 1982 reflecting some improvement in demand and increased shipments for all our products in 1983.
- ☐ The modernized, expanded kraft pulp mill and the new stud lumber mill commenced operations in 1983 and, with the completion of the fine paper machine in March 1984, the Dryden capital programs will be virtually completed.
- ☐ The environmental control programs for Dryden and Thunder Bay to meet government requirements were completed in 1983.

On Inside Pages

Dollars in this report are Canadian unless otherwise identified.

All tons in this report are metric tons. A metric ton is equivalent to approximately 1.1 short tons.

Front Cover

The tree species represented on the cover, jackpine, poplar and spruce, provide the pulps that are used in the manufacture of our fine paper. Deciduous trees such as poplar are referred to as hardwoods while coniferous trees, including jackpine and spruce, are called softwoods. It is the blending of these northern hardwood and softwood species that gives our fine paper its strength and whiteness as well as other printing qualities. Papers manufactured in our Dryden mill are used for the cover of this report and the financial section on pages 9 to 24.

Shareholders' Meeting

Our shareholders' meeting will be held at 11:30 a.m. Eastern Standard Time in the Confederation Room of the Royal York Hotel, Toronto on Monday, April 16, 1984.

TO THE SHAREHOLDERS

The setback we suffered in 1983 was largely due to depressed prices for our major products. Economic conditions are improving, however, and we look for this trend to be reflected in our 1984 results. Despite the adversity in 1983, we are pleased that we were able to maintain dividends although at a reduced rate.

The new Dryden kraft pulp mill facilities went into operation at the beginning of 1983 and, after a brief breaking-in period, performance achieved our best expectations. We were also pleased with the operation of the new stud lumber mill which started up in the second quarter of 1983. Installation of the fine paper machine in Dryden resumed in 1983 and is scheduled for completion in March 1984. This machine, which employs the latest technology, will be an important addition to our manufacturing facilities. Reference to fine paper and the new machine is shown on the front cover, page 1 and page 4 of this report.

In view of the economic difficulties we faced in 1983, we continued our program to reduce capital spending and pare operational costs wherever possible. On behalf of the directors, I would like to extend our sincere appreciation to all employees who contributed to this program by working diligently to improve the efficiency of our operations.

We continued to give full support to the prevention of occupational injury and illness and the control of all other losses which are critical to the success of our company and the personal security of employees and their families. We are encouraged by the progress of this loss control program.

In July 1983 we welcomed Robert W. Campbell, Vice-Chairman and Chief Executive Officer of Canadian Pacific Enterprises Limited, who was appointed a director of the company. He replaced W. John Stenason who resigned in 1983 after 11 years of close association with the company.

On behalf of the directors,

CHARLES J. CARTER,
Chairman and President

Thunder Bay, Ontario
February 1, 1984

LOSS IN 1983 DESPITE HIGHER SALES; OUTLOOK ENCOURAGING

In 1983 we had a loss of $9.9 million or $2.03 per share compared with net earnings of $18.6 million or $3.80 per share in 1982. The loss was mainly due to weak prices for pulp and paper products and increased labor costs. Cost inflation in energy, transportation and chemicals also continued in 1983 and, with the start-up of the Dryden kraft pulp and stud lumber mills, related interest and depreciation charges commenced.

Sales Up

Net sales in 1983 were $495 million versus $437.9 million in 1982. Although pressure on prices continued throughout the year, particularly for kraft pulp and newsprint, shipments of all products were higher in 1983.

Our shipments of kraft pulp recovered substantially in 1983 although there was only a modest recovery in demand for this product. We were able to maintain essentially full operations in the kraft pulp mills, including the expanded Dryden mill. Our ability to produce either softwood or hardwood kraft pulp at one of our Thunder Bay mills enabled us to take best advantage of either of those markets. We also continued development of offshore markets, particularly in the Far East. Kraft pulp prices were extremely depressed throughout 1983, equivalent to those in effect in mid-1979, due to high worldwide inventories and intense competition in the marketplace.

In 1983 full newsprint operations were maintained despite soft market conditions. Excess newsprint manufacturing capacity resulted in widespread erosion of prices. In the second half of the year, however, our price returned to the level which had prevailed through the latter half of 1981 and most of 1982.

Fine paper experienced slack demand in the first half of 1983 but saw substantial market improvement in the last six months with some increases in prices. Installation of the new fine paper machine in Dryden resumed in June and completion is scheduled for March 1984.

North American housing starts in 1983 showed a marked improvement over the previous year. Prices for lumber strengthened considerably during the first half of 1983 and waferboard prices made a modest improvement during the first nine months. However, prices for both products had fallen off by the end of the year due to the re-entry into the marketplace of manufacturing capacity previously idle.

In February 1983 we resumed waferboard operations after a 12-month shutdown. Although profitability was marginal in 1983, we continued operation of this plant in view of the union's agreement to accept lower wage rates. The Dryden stud mill started up late in the second quarter of 1983 replacing the aging dimension lumber mill at Colenso. In November we signed a new agreement to market waferboard through St. Regis Corporation, the same company that handles our stud lumber sales.

Exchange Impact

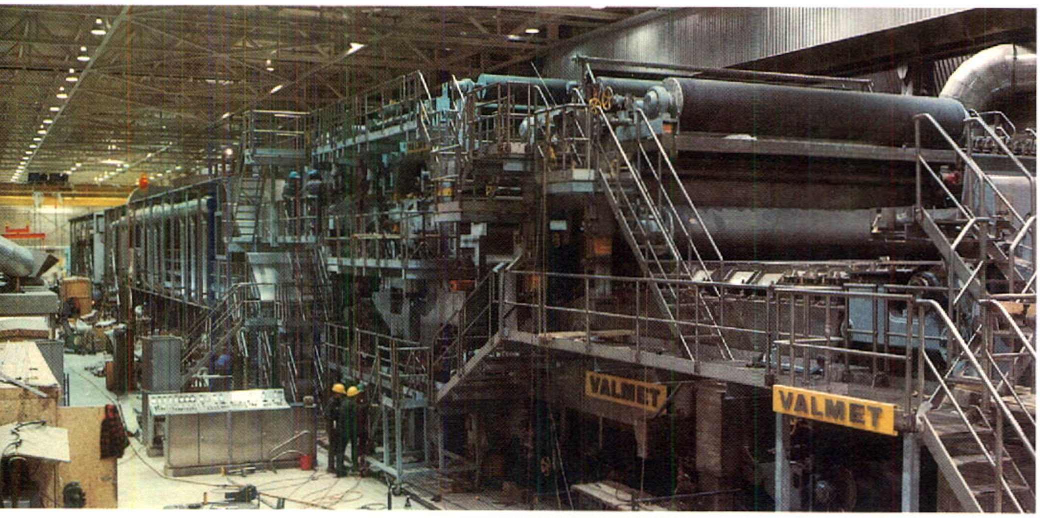
Our average exchange premium on U.S. dollars was 18.7 percent in 1983, down slightly from the previous year. Forward exchange contracts, which were entered into in 1981 for the sale of a substantial portion of our forecast U.S. dollar revenue through 1984, are a major factor in determining our average exchange premium on U.S. dollar sales.

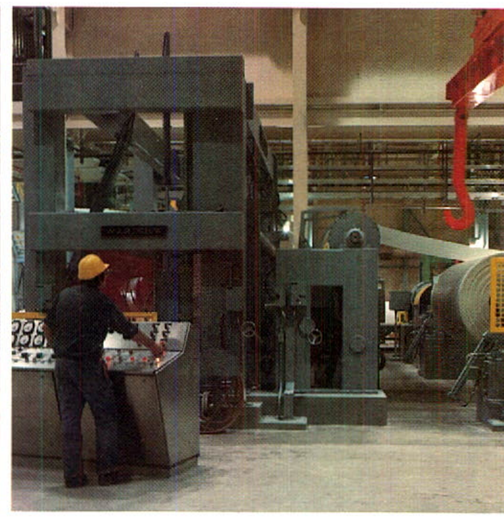
Income Taxes

In 1983 the income tax recovery of $13 million increased from $1.2 million in 1982. In both 1983 and 1982 the basic tax calculation was at a rate of approximately 45 percent. In 1983, taxes so determined were a drawdown from deferred taxes and a credit to earnings due to the company's intention to claim less capital cost allowance for tax purposes than depreciation provided in the financial statements. In 1982 the taxes so determined were a charge to earnings. In both years, investment tax credits earned in the respective years were reflected with the result that in 1983 the basic tax credit to earnings was increased, whereas in 1982 the investment tax credits were sufficiently large due to the heavy capital expenditures on the Dryden modernization program that the credit more than offset the basic taxes.

Dividends

Dividends of $1.20 per share were declared in 1983 compared with $3.20 per share in 1982. The quarterly rate of 30 cents per share was





The new fine paper facilities in Dryden, which are scheduled to start up in March 1984, are shown here as they looked just prior to publication.

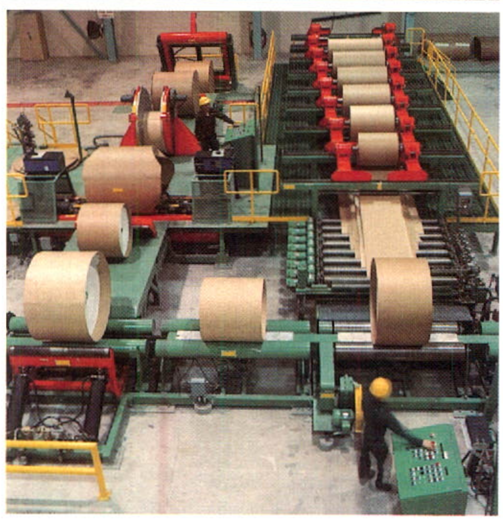
The fine paper machine above is in the final stage of construction. One of the most technologically advanced in the industry, the new machine is 5.5 meters in width and is designed to operate at 15.3 meters per second.

The operator, top right, is testing the winder that will receive the finished paper from the fine paper machine. The winder is designed to operate at a speed of up to 38.25 meters per second. From the winder the paper is fed to the slitters where it is cut into roll sizes suitable for customer requirements or for further processing in our finishing operations.

Bales of hardwood kraft pulp from our Thunder Bay operations are transported to our Dryden facilities and conveyed as shown, far right, to the slusher where they will be blended with softwood kraft pulp from the adjoining Dryden pulp mill. These pulps form the ingredients of our fine paper as discussed in the caption on page 1.

The roll-wrapping system, near right, undergoing a trial run, is designed to handle up to 75 rolls per hour of varying sizes.

The bottom photograph shows the packaging line associated with the cut-to-size sheeter. This automatic equipment cuts sheets of writing or copy paper into letter or legal size, which are gathered in 500-sheet stacks, or reams, and wrapped at a rate of 60 per minute. The machine also automatically packages the reams in cartons and conveys them to a skid ready for shipment.



maintained throughout the year, down from the previous year's quarterly rate of 80 cents per share.

Working Capital Down

Working capital of $26.7 million was down from $49 million in 1982 due to the shortfall of cash generated from operations in meeting capital expenditures, redemption of debt and dividends. A major portion of this shortfall in 1983 was financed by a seven-year fixed-rate term loan from a foreign bank and borrowings under the company's bank line of credit arrangements. Our cash flow from operations was $16.4 million in 1983, down $55.2 million from last year due mainly to the loss in 1983 and a prior year's tax recovery in 1982.

Capital Expenditures

Our capital expenditures in 1983 on all plant facilities and equipment amounted to $56 million. In Dryden, the expanded kraft pulp mill, with an annual capacity of 225,000 metric tons of fully-bleached kraft pulp, commenced operation in mid-January 1983 and the new 60 million board-feet-per-year stud lumber mill went into operation late in the second quarter. This modernization and expansion program, which commenced in 1980, also included extensive environmental control features as discussed in the next section. All these facilities experienced successful start-ups and good operational progress has been made to date. In 1983 capital expenditures for this program were $7.5 million.

The fine paper modernization project in Dryden was resumed in June 1983 after a six-month suspension. The two automatic cutting and packaging lines in the fine paper converting area were in full operation by year end and the fine paper machine is scheduled for completion in March 1984. In 1983 $29.4 million was spent on this project.

In 1983, capital expenditures on the Thunder Bay operations amounted to $15.5 million of which $11.2 million applied to the environmental program to meet government standards as discussed in the next section. The balance was spent primarily to increase energy self-sufficiency and to update newsprint facilities.

Capital expenditures in our Thunder Bay and Dryden woodlands operations amounted to $1.5 million in 1983, primarily for the construction of 142 kilometers of all-weather gravel roads.

Our Environmental Programs

In Thunder Bay's original kraft pulp mill the installation of a new type of pulp washer which separates residual pulping chemicals from the pulp before it proceeds to the bleaching process was successfully started up in September 1983. This completed the last phase in the program of in-plant measures to remove oxygen-consuming wastes from the liquid discharge, or effluent, from the kraft pulp mills before it enters the waterway. To further decrease suspended solids in the effluent, modifications to the existing treatment system were completed in July and additional spill control facilities were operational in September. Improvements to our odor abatement facilities were also completed in 1983.

The new sulphite recovery system in Thunder Bay, which burns spent sulphite pulping chemicals in the kraft mill recovery furnace, was fully operational by September 1983. This system significantly reduced the discharge of oxygen-consuming wastes in the effluent from the sulphite pulp mill in our newsprint operation.

In December 1983 we started up the new filtering system to control emissions to the atmosphere from two main power boilers where the fuel had been switched from natural gas to coal to reduce costs.

In Dryden the secondary effluent treatment system was fully operational by October 1983. The system promotes biological action to treat the effluent through aeration before it is discharged to the river as discussed in the caption on page 7.

The 1983 program completes the installation of environmental control equipment in our Thunder Bay and Dryden operations to meet the requirements of the control orders issued by the Ontario Ministry of the

Environment in 1981 and 1980 respectively. In 1984, in the final phase of our control orders, we will be monitoring our environmental control systems and evaluating their effectiveness.

Our Forest Resources

In June 1983, following 11 years of planning, the Ontario Ministry of Natural Resources published land use guidelines which embrace most of our woodlands areas. While the plans have no legal status, they serve as flexible guidelines for the designation and management of resources to meet the Ministry's resource use targets.

The major impact of the Ministry's plans on our licensed woodlands areas was the withdrawal of a 629 square mile block northwest of Armstrong, Ontario for a wilderness park as shown on the map on the inside back cover. The Ministry also identified additional forest land areas to be withdrawn for a number of waterway parks and nature reserves but the final boundaries have not yet been determined. However, we do not expect the total area to be of the magnitude of the wilderness park. Alienation of forest land from productive uses is a matter of grave concern since it could seriously affect our ability to supply wood fibre to our mills.

Despite the loss of woodlands areas mentioned above, and provided there are no further large withdrawals and proper control of fire and disease is maintained, we are confident that we have sufficient timber to meet our present needs indefinitely. We are encouraged by the Ministry's program of forest management agreements, known as FMA's, which gives the company responsibility for planning and implementing a complete forest management program including harvesting, road construction and regeneration of cutover areas.

In 1983, during our fourth year of operation under the English River Forest Management Agreement, we harvested timber from some 9,300 acres in this area. We seeded approximately 8,745 acres of treated cutover, most of which were harvested in the past few years, and we planted over one million seedlings on 1,900 acres in this management area. An additional 4,230 acres of cutover were treated for aerial seeding to be carried out in the spring of 1984.

In 1984 we expect to sign two more FMA's in our Thunder Bay operating area: one covering working circle 3 and the other covering working circles 5 and 6 combined. The company's 10 working circles are shown on the woodlands map. A third FMA under negotiation in our Dryden woodlands area may be delayed awaiting the public release of the Ministry's land use guidelines for that district. We hope that all our forest areas will be covered by agreements over the next few years.

Employee Relations

In February and March of 1983 two-year agreements, retroactive to 1982, were signed with our woods and office workers respectively thus completing contract negotiations with all unions representing our employees. All our labor agreements expire between April 30 and September 30, 1984.

Market Outlook

The improvement in the U.S. economy which took place in 1983 is expected to continue in 1984 resulting in stronger markets for all our products. There is some concern about the strength of the current recovery but indications are that we can expect the upward trend to continue for the foreseeable future which will help to restore our markets to a normal balance of supply and demand.

With producers' kraft pulp inventories approaching normal levels as we enter 1984 and an anticipated upsurge in the fine paper industry, the major users of bleached kraft pulp, we expect the pulp market to gain strength during the year. Increased prices for kraft pulp went into effect in January 1984. While some new manufacturing capacity will be introduced in mid-year, we do not expect it to upset the stability of the market in 1984. In the following few years, with only minor expansion of pulp production announced and the anticipated improvement of the economy in the U.S. and elsewhere, the kraft pulp market can be expected to resume the healthier growth pattern of previous years.

Secondary treatment of liquid wastes, or effluent, from the Dryden kraft pulp mill is carried out in this man-made lagoon or aeration stabilization basin shown on the left. Following primary treatment to remove suspended solids, the effluent enters the brown area of the lagoon where air is added by means of aerators to promote biological treatment to remove oxygen consuming wastes and leave residual oxygen in the treated effluent. The treated effluent flows from the aeration section to the settling basin in the lower right and from there to the clear area on the left where it enters the outlet at the far end on its way to the river. Average retention time for the liquid in the lagoon is 12 days. The photograph above shows a close-up of an aerator before the lagoon was flooded.

Over the longer term we will continue to experience the usual fluctuations in the market but the increased use of kraft pulp in a wide range of paper products and growing opportunities in offshore markets of the Far East and elsewhere indicate a promising future for this product.

U.S. newsprint consumption was 10.6 million metric tons in 1983 compared with 10.1 million metric tons in 1982, the first significant increase in five years. Late in 1983 the newsprint market gained strength and this trend is expected to continue in 1984. At year end, inventories in customers' hands were approaching normal levels. As well as the projected strengthening of the U.S. economy, other factors will affect demand for newsprint in 1984. With the possibility of labor disruptions as a result of contract negotiations in Canada, publishers can be expected to stockpile newsprint during the year and 1984 is an election year in the U.S. which should result in increased newsprint usage. During the next few years we believe that the market for newsprint will respond favorably to the anticipated improvement in the economy and the impact of major increases in productive capacity which took place over the past five years is expected to wane. Over the longer term we believe that the demand for newsprint will continue to grow providing increased marketing opportunities.

We entered 1984 with a strong demand for fine paper. This was a substantial improvement over the past few years and we expect the market to remain strong throughout the year. Over the next few years, in line with the anticipated economic improvement, the outlook for fine paper is positive. Looking to the future, there is every indication that the demand for fine paper will continue to grow offering encouraging prospects for this product.

The substantial improvement in house-building activity in 1983 is expected to continue in 1984. With this anticipated improvement, the market for stud lumber and waferboard, the latter emerging as a major competitor to plywood, is expected to strengthen although increased operating rates will result in strong competition. We expect the demand for building products will continue to grow over the longer term with the inevitable soft periods as we have experienced in the past.

Company Outlook

The projected strengthening of our markets in 1984 will have a favorable effect on our results, particularly with the prospect of increased prices for our products. While an improvement in economic conditions is projected it may be another year or so before our markets will reach their full potential. Our new fine paper machine will start up in the first quarter at a time when the market for that product is expanding. On the negative side, we must consider the inevitable increase in operating costs during the year which will undermine our market gains. On balance, assuming the orderly completion of negotiations with our unions, we look for steady progress in 1984 which should be reflected in positive results.

The new Dryden facilities are modern and diversified and complement our Thunder Bay operations which have been improved and updated over the years. Also, our Dryden and Thunder Bay woodlands operations are highly mechanized and as modern as any to be found. To maintain our operations at a high level of efficiency we provide training programs for our employees to upgrade their skills and prepare for technological change. With our first-rate facilities and skilled work force we are able to produce quality products and meet the competitive challenge we will encounter over the next few years as we recover from the recent recession.

The heavy investment in our undertakings over the past few years was burdensome, but it is now behind us. We believe that our strong position will stand us in good stead as we ride the crest of future opportunities and hold our own during periods of adversity. Those who participated in the development of our company in recent years can look back with satisfaction at what has been accomplished and look forward to sharing in the benefits of a healthy, growing enterprise.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF 1983 FINANCIAL STATEMENTS

Operating Results

Net sales of $495 million in 1983 were $57.1 million higher than in 1982. This resulted from higher shipment volumes for all products increasing net sales by $102.9 million and lower average selling prices eroding this by $45.8 million. The higher volumes were provided by increased capacities for kraft pulp and stud lumber from new facilities in Dryden, resumption of the waferboard operation in Thunder Bay after having been shut down for virtually all of 1982 and higher operating rates for all of the company's mills. Increased deliveries of all products to the company's traditional market areas were augmented by higher volumes of kraft pulp shipments to the Far East and increased sales to serve a growing demand for hardwood kraft pulp. Unfortunately, the improvements in market demand evidenced by increased shipments in 1983 did not reflect similarly in prices for the company's principal pulp and paper products. Intense competition in the marketplace throughout 1983 resulted in average prices for softwood and hardwood kraft pulp decreasing by 12 percent and 8 percent respectively, and average newsprint prices were lower by 2 percent. Lumber prices strengthened considerably during the first half of 1983 and improvements also occurred in waferboard prices. Most of these gains, however, were lost by the end of the year as additional production entered the market. The only product which experienced sustained strengthening of prices was fine paper where modest increases occurred in the latter half of the year. Due to the higher sales revenue, forward exchange contracts which were negotiated in 1981 and extend through 1984 covered 78 percent of U.S. dollar sales proceeds in 1983 versus 82 percent in 1982. The exchange premium experienced by the company is largely determined by these contracts and averaged 18.7 percent in 1983 compared with 19.1 percent in 1982.

Cost of sales of $446.5 million increased $75.8 million in 1983 due primarily to the higher shipment volumes. Essentially full operation of all facilities in 1983, including waferboard after it resumed operation in mid-February, contrasted with the periodic shutdowns experienced in 1982. As a result, operating efficiencies partially offset continued escalation in labor, energy and transportation rates in 1983. In addition, significant cost reductions were realized from operation of the new kraft pulp mill in Dryden throughout 1983. Selling and administrative expenses increased by $3.1 million to $13 million in 1983 due to selling costs associated with increased pulp shipments and higher stud lumber and waferboard shipments. Throughout 1983 the company continued its efforts to contain overhead and administrative expenses with the result that these costs were relatively unchanged from 1982. Interest on borrowed funds rose $6.7 million to $23.1 million in 1983 due to higher debt levels. However, interest charged to earnings increased by $11.1 million to $17.7 million since interest on funds borrowed to finance the new kraft pulp mill in Dryden was no longer capitalized in 1983. The remaining interest of $5.4 million in 1983 has been capitalized in connection with the fine paper machine which is not yet completed. A $2.3 million exchange adjustment was charged to earnings in 1983 to record the 8¾ percent debentures payable in U.S. funds at the current exchange rate since this issue matures in early 1984 and is classified as a current liability. Depreciation expense of $39.9 million increased by $6.2 million in 1983 due to the additional depreciation associated with the new kraft pulp mill and stud lumber facilities in Dryden. The income tax recovery increased from $1.2 million on pre-tax earnings of $17.4 million in 1982 to $13 million on a pre-tax loss of $22.9 million in 1983. In both years, taxes were provided at approximately 45.5 percent, although in 1982 they were a charge against pre-tax earnings and in 1983 they are a recovery of deferred taxes previously provided. Additionally, in 1982, the substantial investment tax credits generated by the heavy capital expenditures on the Dryden kraft pulp mill more than offset the tax provision mentioned above to produce a small net recovery. In 1983 the investment tax credits are less and add to the tax recovery already provided.

The paper in this section is opaque litho made in our Dryden fine paper mill.

Financial Condition

Working capital decreased $22.3 million in 1983, from $49 million to $26.7 million. The principal changes within working capital are: an increase of $18.9 million in accounts receivable due to the higher volume of shipments in 1983, the refund of $21.7 million of income taxes paid in 1981, an increase of $10 million in accounts payable due to a higher level of activity, a reduction of $10.4 million in the amount drawn down under the line of credit with Canadian Pacific Securities Limited and an increase of $13 million to reflect the current maturity of the 8¾ percent debentures in early 1984. Cash flow from operations in 1983 was $16.4 million, down $55.2 million from 1982. The principal reasons for the reduction were the decrease in net earnings by $28.5 million and the fact that the tax recovery for 1983 is essentially all deferred whereas a tax-loss in 1982 generated a $21.7 million recovery of taxes paid in 1981. During 1983 the final payments totalling $4.7 million were received under the $48 million of government grants awarded to the company for the various modernization and environmental programs undertaken since 1980. These programs, when completed in early 1984, will aggregate approximately $450 million. Capital expenditures in 1983 amounted to $56 million, of which $7.5 million applied to the new Dryden kraft pulp and stud lumber mills, $29.4 million to the Dryden fine paper machine, $11.2 million to environmental improvements in Thunder Bay and the remainder to woodlands and minor mill projects. During the year the company borrowed $30.9 million (U.S. $25 million) under an unsecured term loan from a foreign bank for seven years. In addition, the company drew down a further $5 million under its existing Canadian bank lines of credit. As at December 31, 1983 the ratio of debt to debt plus equity was 41.6 percent compared to 38.1 percent the previous year and floating rate borrowings represented 56 percent of total debt, down from 65 percent at the end of 1982.

Effects of Economic Conditions

The company incurred a loss of $9.9 million in 1983 compared with net earnings of $18.6 million in 1982. The reason for the loss was that depressed kraft pulp and newsprint prices, which reached a low point in the fourth quarter of 1982, continued throughout 1983 with only minor recovery for newsprint at mid-year. At year end newsprint prices equate to mid-1981 prices and kraft pulp prices equate to mid-1979 prices. With the relentless increase in labor, energy and transportation costs, even with the efficiencies resulting from higher operating rates, new facilities and cost containment measures, the price of kraft pulp, the company's principal product, was not high enough to recover its costs of administration, interest and depreciation. The signs of strengthening of markets for the company's products, evidenced by increased demand in the latter part of 1983, are expected to extend to price improvements, particularly for kraft pulp, in 1984. Also, the completion of the Dryden fine paper machine will result in expanded capacity for that product in 1984, although additional depreciation and interest expense will have to be absorbed when that facility comes into operation. As the effects of economic recovery in North America work their way through to the pulp and paper and building products commodities, the expectation is for improved results in 1984. In the meantime, the company will continue to curtail discretionary capital expenditures and will make every effort to control administrative costs.

Inflation Accounting

The position adopted by this company with respect to the recommendations of the Canadian Institute of Chartered Accountants on inflation accounting are explained in a separate presentation on page 18 following the notes to the financial statements.

AUDITORS' REPORT TO THE SHAREHOLDERS

To the Shareholders of Great Lakes Forest Products Limited

We have examined the consolidated balance sheet of Great Lakes Forest Products Limited as at December 31, 1983 and the consolidated statements of earnings, 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 on a basis consistent with that of the preceding year.

Thorne Riddell

THORNE RIDDELL
Chartered Accountants

Toronto, Canada, January 21, 1984

EARNINGS

consolidated statement for years ended December 31 (thousands of dollars)

	1983	1982
Net sales:		
Pulp and paper	$453,185	$416,246
Building products	41,796	21,608
	494,981	437,854
Cost of sales	446,511	370,690
Selling and administrative expense	13,041	9,961
OPERATING PROFIT	35,429	57,203
Interest and other income	1,484	1,355
	36,913	58,558
Interest (Note 5)	17,679	6,630
Foreign exchange on long-term debt	2,272	877
Depreciation	39,863	33,701
EARNINGS (LOSS) before income taxes	(22,901)	17,350
Income taxes (Note 6)	(12,965)	(1,202)
NET EARNINGS (LOSS)	$ (9,936)	$ 18,552
Net earnings (loss) per share	$ (2.03)	$ 3.80

RETAINED EARNINGS

consolidated statement for years ended December 31 (thousands of dollars)

Retained earnings at beginning of year	$278,298	$275,376
Net earnings (loss)	(9,936)	18,552
	268,362	293,928
Dividends declared	5,862	15,630
RETAINED EARNINGS at end of year	$262,500	$278,298

BALANCE SHEET

consolidated statement at December 31 (thousands of dollars)

	1983	1982
Assets		
CURRENT ASSETS		
Cash	$ 121	$ 3,701
Accounts receivable	66,867	48,004
Income taxes recoverable	—	21,670
Inventories:		
Finished goods	8,942	9,360
Pulpwood and sawlogs	34,968	36,641
Materials and supplies	29,080	29,563
Prepaid expenses	1,818	2,823
	141,796	151,762
FIXED ASSETS (Note 2)	892,490	844,613
Accumulated depreciation	309,232	272,183
	583,258	572,430
	$725,054	$724,192

	1983	1982
Liabilities		
CURRENT LIABILITIES		
Accounts payable and accrued charges	$ 51,080	$ 41,089
Loan payable (Note 10)	38,000	48,373
Income and other taxes payable	8,789	6,674
Dividend payable	1,465	3,907
Current portion of long-term debt	15,767	2,728
	115,101	102,771
LONG-TERM DEBT (Note 3)		
First Mortgage Bonds:		
8% sinking fund bonds, Series B, maturing 1989	10,002	10,808
11¼% sinking fund bonds, Series C, maturing 1995	29,264	30,380
8¾% debentures maturing 1984 (U.S. $11.6 million)	12,143	12,143
Term loan (U.S. $25 million)	30,860	–
Notes payable	11,430	14,306
Lease obligations	2,497	4,968
Bank loans	89,161	84,144
	185,357	156,749
Current portion	13,495	2,728
	171,862	154,021
DEFERRED INCOME TAXES	120,942	134,453
Shareholders' Equity		
Common shares		
Authorized 10,000,000 shares		
Issued 4,884,355 shares	54,649	54,649
Retained earnings	262,500	278,298
	317,149	332,947
	$725,054	$724,192

Approved by the Board:

C. J. CARTER, *Director*

RICHARD C. MEECH, *Director*

CHANGES IN FINANCIAL POSITION

consolidated statement for years ended December 31 (thousands of dollars)

	1983	1982
WORKING CAPITAL PROVIDED		
Net earnings (loss)	$ (9,936)	$ 18,552
Items not affecting working capital:		
Depreciation	39,863	33,701
Deferred income taxes	(13,511)	19,369
GENERATED FROM OPERATIONS	16,416	71,622
Government grants	4,693	4,856
Issue of long-term debt	35,877	88,004
Sale of fixed assets	639	499
	57,625	164,981
WORKING CAPITAL USED		
Expenditures on fixed assets	56,023	168,765
Reduction of long-term debt	18,036	9,580
Dividends declared	5,862	15,630
	79,921	193,975
DECREASE IN WORKING CAPITAL	22,296	28,994
Working capital at beginning of year	48,991	77,985
WORKING CAPITAL at end of year	$ 26,695	$ 48,991

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Year ended December 31, 1983

1. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the financial position and results of operations of Great Lakes Forest Products Limited and all its subsidiary companies.

Foreign Exchange

Accounts receivable and sales in U.S. dollars, to the extent that they are covered by forward exchange contracts, are converted at the rates of exchange provided in the contracts. Other current assets and current liabilities in foreign currencies are translated into Canadian dollars at current rates of exchange at the date of the balance sheet. Other assets and liabilities and items affecting earnings are converted at rates of exchange in effect at the dates of the transactions.

Inventories

Inventories of finished goods and materials and supplies are valued at the lower of average cost and net realizable value. Inventories of pulpwood and sawlogs are valued at average cost.

Fixed Assets and Depreciation

Fixed assets are recorded at cost which is net of the proceeds of government grants. The cost and related accumulated depreciation of items disposed of are removed from the accounts and any gain or loss is included in earnings. Depreciation is based on the estimated economic lives of the assets, using the following methods and composite rates of depreciation:

Buildings and machinery	
Pulp and paper	4½% straight line
Building products	10% straight line
Woodlands improvements and equipment	30% diminishing balance

No depreciation is charged on major improvements or expansions until construction has been completed.

Capital Leases

Assets under capital lease are capitalized at their fair value at the inception of the lease. The related obligation is recorded as long-term debt and represents the present value of minimum lease payments. The assets are depreciated in accordance with the depreciation policy stated above and the implicit interest content of the lease payments is charged to earnings as interest on long-term debt.

Income Taxes

The company follows the tax allocation method in accounting for income taxes. Under this method, deferred income taxes are recorded to reflect the tax effect of timing differences between reported and taxable income. The principal timing difference results from the claiming of capital cost allowance for tax purposes either greater or less than the depreciation charged to earnings and consequently deferred income taxes may be either a charge or a credit to earnings.

Investment tax credits are recognized in the year in which the qualifying capital expenditures are made. These tax credits affect taxable income of future years since the value of depreciable assets for taxation purposes is reduced by the amount of the credits claimed as a reduction of income taxes payable. A portion of the tax credits, determined at the current tax rate, is therefore set aside as deferred income taxes and the balance is applied to reduce income taxes charged to earnings.

Interest

Interest on debt incurred to finance major expansion programs, less any interest earned on the temporary investment of the proceeds, is capitalized during the construction period.

Net Earnings Per Share

Net earnings per share are calculated based on the average number of shares outstanding during the year.

2. Fixed Assets (thousands of dollars)

	December 31, 1983 Cost	December 31, 1983 Net Value	December 31, 1982 Net Value
Land	$ 1,495	$ 1,495	$ 1,325
Buildings and machinery			
Pulp and paper	649,799	433,015	291,299
Building products	45,641	21,961	6,217
Woodlands improvements and equipment	79,754	21,017	26,620
Timber licences	3,945	–	–
Assets under capital lease	7,120	1,034	2,872
Construction in progress	104,736	104,736	244,097
	$892,490	$583,258	$572,430

3. Long-Term Debt

The company has an unsecured term loan from a foreign bank in the amount of $25 million (U.S. funds) repayable on April 6, 1990 with interest thereon at the fixed rate of 11.94 percent per annum payable annually.

The notes payable are to two non-resident suppliers of equipment and contain terms and conditions which are similar and maturity dates which are two months apart. The terms and conditions of the larger of the two notes provide for interest at the rate of 10 percent with the principal to be repaid in 10 semi-annual installments to August 1987.

Repayment of these notes has been arranged through a foreign bank which extends the terms of repayment to 1989, with the right of prepayment.

Obligations under capital leases comprise many individual leases with implicit interest rates ranging from 6 percent to 12 percent with expiry dates extending to 1989.

Loan agreements with two Canadian banks currently provide for operating lines of credit of $80 million in either U.S. or Canadian funds at floating rates. Loans are secured by charges on inventory and assignments of accounts receivable. These agreements expire on June 1, 1985. As at December 31, 1983 $25 million in Canadian funds was drawn down under these agreements.

In addition, the company has loan agreements with two other banks for unsecured operating lines of credit totalling $100 million (U.S. funds or Canadian equivalent) at floating or fixed interest rates. The revolving credit periods under these agreements expire on June 30, 1986 and December 30, 1990 respectively. Amounts then outstanding convert to term loans extending to June 30, 1990 and December 30, 1993. As at December 31, 1983 $50.8 million in U.S. funds was drawn down under these agreements.

Required payments to reduce long-term debt over the next five years, based on the exchange rates at which the debt is recorded in the financial statements, are as follows (thousands of dollars):

	Bonds and Debentures	Bank Loans	Other	Total
1984	$14,415	$ –	$ 1,352	$15,767
1985	2,086	25,000	462	27,548
1986	2,620	6,416	460	9,496
1987	2,870	14,950	304	18,124
1988	3,150	17,067	5,912	26,129

4. Dividend Restriction

Certain of the indentures relating to the company's long-term debt contain covenants limiting dividends. The most restrictive of these requires that, after any dividend is declared, working capital (which for these purposes is before the deduction of the current portion of long-term debt) must be over $10 million and shareholders' equity must be over $50 million.

5. Interest

Interest for the year amounted to $19.2 million ($15.1 million in 1982) on long-term debt and $3.9 million ($1.3 million in 1982) on short-term indebtedness. Of these amounts, $5.4 million ($9.8 million in 1982) has been capitalized.

6. Income Taxes

The company has provided for income taxes (recoveries) resulting in the following effective rates:

	1983	1982
	thousands of dollars	
Earnings (loss) before income taxes	$(22,901)	$17,350
	percent	
Combined basic federal and provincial rate		50.0 %
Manufacturing and processing allowance		(6.0)
Federal 5% surtax		1.5
		45.5
Deferred tax drawdown rate (average of rates for accumulations in prior years)	(45.4) %	
3% inventory allowance	(2.8)	(3.8)
Federal investment tax credits	(12.4)	(49.1)
Other	4.0	.5
Effective rate of income tax (recovery)	(56.6) %	(6.9) %

7. Past Service Pension Costs

Past service pension costs, resulting from retroactive increases in benefits in the current and prior years, are being funded and charged to earnings over 15-year periods from the dates such costs were established. Based on actuarial valuation of the employees' pension plans as at January 1, 1983, the unfunded amount as at December 31, 1983 is estimated to be $10 million.

8. Forward Exchange Contracts

The company has entered into forward exchange contracts for the delivery of $360 million U.S. funds to the end of 1984 at exchange rates which average $1 U.S. = $1.174 Cdn.

9. Litigation

The agreement under which the company purchased the assets of the Dryden operations of Reed Ltd. in 1979 provides that the company and Reed Ltd. shall share equally any liability up to $15 million plus related costs arising from claims, actions or proceedings based on actions, circumstances or events up to the date of purchase and related to the discharge, escape or presence of any pollutant from or in the assets purchased by the company. Amounts payable by Reed Ltd. pursuant to the foregoing have been unconditionally guaranteed by Reed International Limited (the United Kingdom-based senior company in the Reed group of companies). In the event that any liability in excess of $15 million plus related costs were to arise, the company would be responsible.

Legal proceedings based on alleged pollution are as follows:

a) two actions instituted by writs dated in 1970 by Barney's Ball Lake Lodge Limited and by Ontario Central Airways Limited against Dryden Chemicals Limited and Dryden Paper Company Limited (predecessor companies to Reed Ltd.) claiming damages said to be caused by alleged pollution of the Wabigoon-English River system. No proceedings have been taken in the Airways action and the last proceedings in the Lodge action was examination for discovery of the President of the plaintiff in 1971. The examination for discovery was adjourned pending production by the plaintiff of further information, which information has not been produced. The amount of damages claimed in the Lodge action total $3.8 million and no amount has been specified in the Airways action. It is not possible to make any firm estimate of the damages sustained or the ultimate liability, if any, should these actions proceed.

b) an action instituted by writ dated in 1977 on behalf of numerous plaintiffs, members of two Indian bands, against Reed Ltd. and its predecessor companies, claiming damages said to be caused by alleged pollution of the Wabigoon-English River system and requesting a mandatory order requiring removal of the alleged pollutants. A statement of claim has not been filed nor have any proceedings on this action been taken and it is not possible to make any firm estimate of the damages sustained or the ultimate liability, if any, should this action proceed.

The Treasurer of Ontario wrote to the company in 1979 stating in paragraph 2, "I further understand that the Reed group of companies and Great Lakes are willing to assume, on an equal basis, responsibility, up to a maximum of $15 million, for any environmental damages attributable to the operations of Reed Ltd. or any of its predecessor companies in the Dryden area prior to this acquisition by Great Lakes". The letter further states, "... in the event that Great Lakes is required to pay any monies as a result of any final decision of a court against Great Lakes, Reed Ltd. or any other person prior to the year 2010 in respect of pollution caused by Reed Ltd. or any of its predecessor companies in the Dryden area prior to the date upon which Great Lakes acquires the assets and undertaking of the Dryden complex of Reed Ltd. or in the event that any settlement with any claimant is made the amount of which settlement has been approved by the Attorney General of Ontario, I have been authorized by the Executive Council of Ontario to advise you that I will make a Recommendation to the Executive Council of Ontario that the Government of Ontario take effective steps to ensure that Great Lakes Forest Products Limited will not be required to pay any monies in excess of the maximum amount of $15 million referred to in paragraph 2 of this letter, provided that over the next three to four years Great Lakes expends in the order of $200 million for the modernization and expansion of the Dryden facilities". The position of the Government of Ontario was confirmed in a letter to the company from the Provincial Secretary for Resources Development dated January 28, 1982.

Any material payment by the company related to these actions is expected to be accounted for as an adjustment of the purchase price of the Dryden assets.

10. Related Party Transactions

Canadian Pacific Enterprises Limited owns approximately 54 percent of the common shares of the company and consequently the many companies within the Canadian Pacific organization are related parties.

The company has a revolving line of credit with Canadian Pacific Securities Limited in the amount of $50 million (Canadian funds or U.S. equivalent) which provides for loans of up to one year at interest rates based on the lender's cost of borrowing. At December 31, 1983 $38 million in Canadian funds was drawn down under this line of credit. Interest for the year under this line of credit amounted to $3.9 million.

The company makes extensive use of both major Canadian railways, including C.P. Rail for the transportation of its inbound pulpwood and outbound finished products. Freight rates are at published tariff rates.

A small portion of the company's production is sold to subsidiaries of CIP Inc., a subsidiary of Canadian Pacific Enterprises Limited. Such sales are made in accordance with the company's normal terms of sale.

In addition, in the normal course of business, the company makes use of other services, facilities and products of the Canadian Pacific organization. These transactions are, to the knowledge of management, at terms and rates no more nor less favorable than with unrelated parties.

11. Industry Segment and Export Sales

The company's entire operations consist of the manufacture and sale of products of the forest industry. In both 1983 and 1982, 86 percent of the company's net sales were exported, largely to United States destinations, and priced in U.S. dollars.

INFLATION ACCOUNTING

For several years, the company has expressed reservations about the appropriateness of attempting to quantify the effects of inflation within the framework of corporate financial statements. As we explored the various methods proposed in this country and others, we became concerned about the ability of users of financial statements to understand some of the complex concepts introduced and to appreciate the implications and limitations inherent in such information. For this reason our position has been to avoid the confusion of experimentation pending the emergence of some system meeting the criteria of simplicity and uniformity of application for the preparers of financial statements and capable of achieving a level of general understanding by the readers of financial statements.

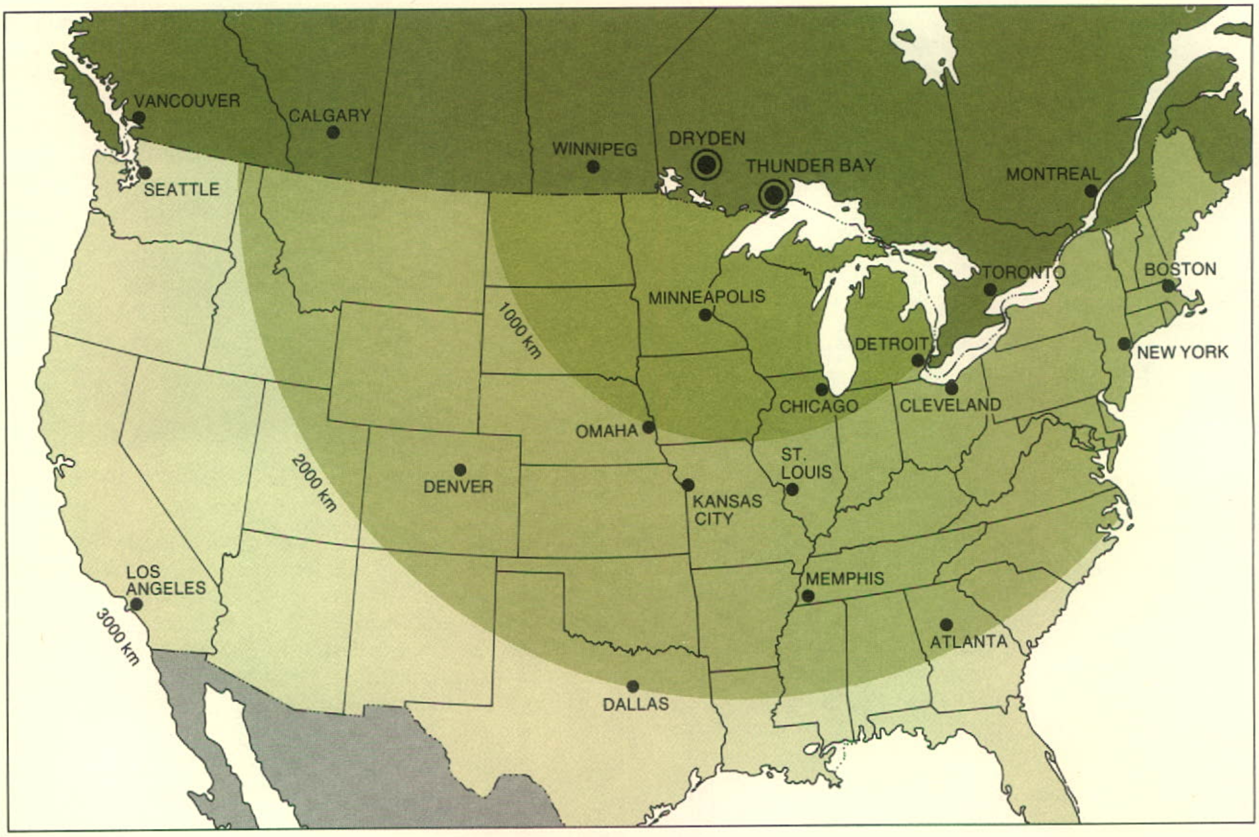
The Canadian Institute of Chartered Accountants has issued its recommendations on reporting the effects of changing prices and encourages adoption by most large public companies commencing with the 1983 year. The recommendations call for inclusion of certain supplementary information directed toward the two principal concepts of maintaining the operating capability of the enterprise and maintaining the general purchasing power of its capital, free of the effects of inflation. By so doing, the information purports to establish a commonality which better enables comparability and performance evaluation between enterprises and within enterprises across time periods.

We have experimented with various approaches to meet the requirements of the C.I.C.A. standard and have succeeded only in reinforcing our doubts about the usefulness of the information developed. In an inflationary environment, any exercise designed to eliminate the effect of changing values from historical cost financial statements would likely establish that a company's principal assets, normally its inventories and fixed assets, are understated in terms of their current or replacement costs. It follows that traditionally reported earnings would be overstated since charges reflecting the use, consumption, depreciation or amortization of those assets would be understated in terms of current costs. While these conditions would be entirely valid for Great Lakes Forest Products Limited, the problem arises in quantifying the adjustments and interpreting their significance.

For most capital-intensive manufacturing concerns, the determination of the replacement cost of the fixed assets becomes critical to the integrity of the entire exercise. The pulp and paper industry is characterized by large, complex mills constructed and expanded over extended periods of time and often employing technologies which have undergone significant changes over the years. Also, replacement of these facilities today would be subject to intense environmental scrutiny. A major weakness, therefore, in the concept of establishing the replacement cost of existing facilities is the likelihood that a company could not, would not, or would not be permitted to replace its facilities as they presently exist. At best, it would be possible to estimate the current capital cost of new facilities having similar productive capacities, but these would likely employ different production and environmental technologies with operating costs and efficiencies the effects of which we are not able to measure. Alternatively, it would be possible to apply construction cost escalation indices to the historical costs, but generalized indices when applied to large numbers over long time periods may not be representative of current costs. Another matter which the forest products industry is not able to address is the valuation of its most precious asset; its fibre resource. Some companies own their harvestable forest resource, others have long-term cutting rights on Crown-owned land, and others are supplied by the residue from another company. Regardless of which is the case, and whether or not any cost appears on a company's historical cost balance sheet, the importance of this resource is such that companies today are often bought solely on the basis of their access to wood fibre. Unfortunately, it does not seem possible, and the C.I.C.A. offers no proposal, to determine a current value that has any degree of comparability within the industry for a resource, which, in a concept of economic values, probably represents its most important asset. Solutions to these and other problems in the determination of current cost data must be developed on the basis of assumptions and subjective estimates that are not verifiable and the adoption of different, but equally valid, assumptions would produce materially different results.

We have concluded that the C.I.C.A. recommendations for reporting the effects of changing prices fail to meet the objectives of simplicity, uniformity and understandability to which we could subscribe. The exercise produces information which has the appearance of authority but which our experimentation reveals contains substantial subjective valuations and assumptions which undermine its credibility. Conceptually, it pits the intangibles of economic theory against the pragmatics of accounting principles and we have been unable to interpret the significance of the resulting differences. For these reasons, we do not believe that the supplementary information recommended by the C.I.C.A. would be useful to the readers of our financial statements in assessing the performance or future prospects of the company. We have therefore not included the recommended supplementary information.

OUR MARKETS



The Thunder Bay and Dryden mills are well situated to serve North American markets. The bulk of our production reaches customers within a radius of 2,000 kilometres of our mills. Virtually our entire newsprint market at present lies within this area. The largest portion of our kraft pulp production also reaches this area. However, a significant volume is shipped to areas such as California and offshore markets including the Far East. Some of our fine paper production is shipped to the midwestern United States but the majority is shipped to markets in Canada. The bulk of our building products is sold to customers in the United States within the 2,000 kilometre range and to customers in Canada.

OUR SHIPMENT SUMMARY: LAST FIVE YEARS

	1979	1980	1981	1982	1983
Newsprint (thousands of metric tons)	378	391	386	360	393
Kraft pulp (thousands of metric tons)	356	521	504	380	531
Fine papers (thousands of metric tons)		62	64	44	46
Total (thousands of metric tons)	734	974	954	784	970
Lumber (millions of board feet)	107	132	137	114	137
Waferboard (millions of sq. ft.—3/8-inch basis)	111	87	86	15	73

While waferboard is manufactured in varying thicknesses, for comparative purposes with the industry statistics on page 21, our shipment volume is shown here on a 3/8-inch equivalent basis.

NEWSPRINT PAPER

The United States is Canada's principal customer for newsprint and accounts for approximately 46 percent of the free-world's consumption. The following table, based on reports issued by the Canadian Pulp and Paper Association (CPPA), indicates the size and growth of newsprint markets over the period 1979 through 1983. World totals for newsprint omit communist countries for which reliable information is lacking.

	1979	1980	1981	1982	1983
		(millions of metric tons)			
Free-world production capacity	23.8	24.9	26.0	27.5	28.0
Free-world production	22.2	23.0	24.1	22.5	23.4
Canadian production capacity	9.1	9.1	9.5	9.9	10.0
Canadian production	8.8	8.6	8.9	8.1	8.5
Canadian exports	7.8	7.6	7.9	7.1	7.5
Canadian exports to U.S.	6.4	6.1	6.1	5.6	6.0
Total U.S. consumption	10.2	10.1	10.2	10.1	10.6

Source: CPPA (1983 estimated).

BLEACHED KRAFT PULP

Bleached kraft pulp is included in the general commodity classification of paper grade chemical pulp. North America and Scandinavia are the major suppliers of paper grade chemical pulp, having a production capacity in 1983 of approximately 65.0 million metric tons or 65.6 percent of the world's total production capacity. The bulk of the pulp produced by these countries is captive production for use by the producers or affiliated companies. The balance, known as market pulp, is available for sale on the open market. Most of this market pulp consists of bleached kraft pulp. In 1983 the production capacity in North America and Scandinavia for market bleached kraft pulp was approximately 15.7 million metric tons of which Canadian production capacity amounted to approximately 41.1 percent, or 6.4 million metric tons. Our company is a major supplier of this market pulp.

	1979	1980	1981	1982	1983
Paper Grade Chemical Pulp		(millions of metric tons)			
North American and Scandinavian production	58.7	59.4	59.9	55.2	60.0
Bleached Kraft Pulp					
North American and Scandinavian production	29.6	31.0	31.7	30.4	33.6
Market Bleached Kraft Pulp					
Total demand for North American and Scandinavian production	12.6	13.3	13.0	11.8	14.1
Canadian shipments	5.4	5.9	5.5	4.7	5.8
Canadian exports to U.S.	2.0	2.0	1.9	1.6	2.0
Total U.S. supply (including imports)	4.0	4.0	3.9	3.6	4.4

Source: CPPA (1983 estimated).

FINE PAPER

The term "fine paper" covers a broad range of papers manufactured to suit a variety of specialty end uses. The major categories are: converting papers, which include papers used for envelopes, scribblers and continuous and single multiple-part forms, representing approximately 40 percent of all fine papers produced in Canada; printing grades, representing 40 percent, which include coated and uncoated papers designed specifically for the printing of text books, annual reports, magazines, advertising pieces, etc.; and business papers, representing 20 percent, which include papers for office copiers, letterheads, documents, office forms, etc.

At our Dryden mill we manufacture only a few fine paper products in the above categories, primarily those classified as uncoated printing papers, copy papers and envelope papers.

	1979	1980	1981	1982	1983
			(thousands of metric tons)		
Canadian production capacity	943.0	982.0	1,019.0	1,008.0	1,026.0
Domestic shipments	704.4	697.2	661.6	648.8	718.8
Export shipments	204.1	200.8	127.2	174.1	238.4
Canadian imports	130.0	150.9	217.7	153.3	185.0
Canadian demand	834.4	848.1	879.3	802.1	903.8

Sources: Statistics Canada, CPPA (1983 estimated).

LUMBER

Residential construction provides the principal use for softwood lumber produced in Canada and the U.S., a substantial portion of which is stud lumber. The following table indicates the level of housing construction and the sources of softwood lumber production in North America over the past five years.

	1979	1980	1981	1982	1983
			(millions)		
North American housing starts	1.9	1.5	1.3	1.2	1.9
Seasonally adjusted year-end rate of North American housing starts	1.7	1.7	1.1	1.4	1.8
Softwood lumber production			(billions of board feet)		
U.S.	29.7	31.6	22.8	21.0	25.5
British Columbia	12.5	12.0	10.4	9.9	12.2
Rest of Canada	6.0	6.2	6.0	5.3	6.5
Total	48.2	49.8	39.2	36.2	44.2

Sources: Statistics Canada, U.S. Bureau of Census, National Forest Products Assn. (1983 estimated).

BOARD

Waferboard competes in its uses with the exterior grades of softwood plywood sheathing which represent approximately 75 percent of all softwood plywood production in North America.

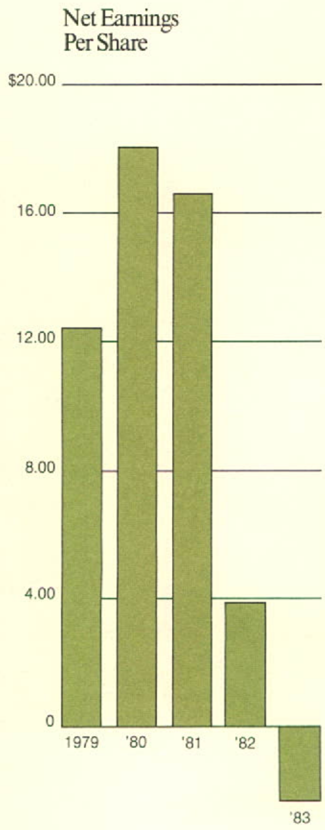
	1979	1980	1981	1982	1983
			(billions of square feet)		
Softwood plywood (⅜-inch basis)					
U.S. production	19.7	16.7	17.1	17.0	21.0
Canadian production	2.8	2.6	2.4	1.9	2.1
Waferboard (⅜-inch basis)					
Canadian production	.6	.6	.8	.6	.8
U.S. production	.1	.2	.3	.6	1.2

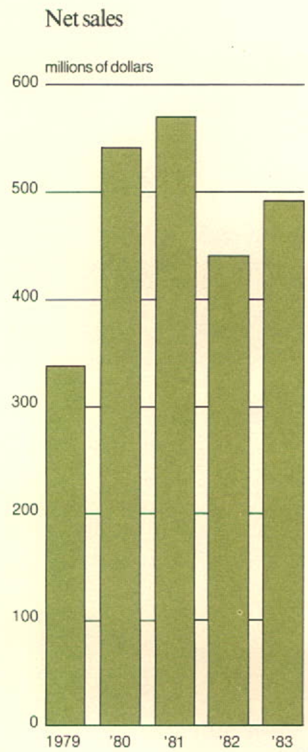
Sources: Dept. of Industry, Trade and Commerce, American Plywood Assn., FORSIM of Data Resources Inc. (1983 estimated).

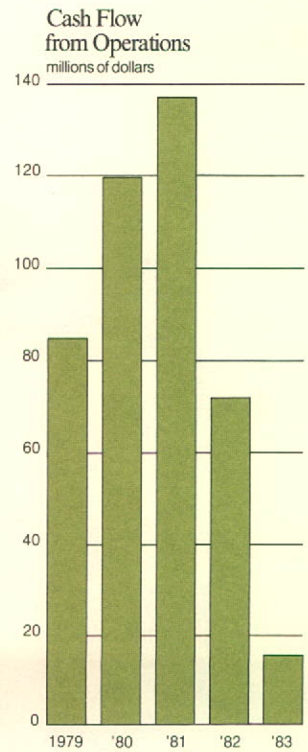
FINANCIAL SUMMARY: LAST FIVE YEARS

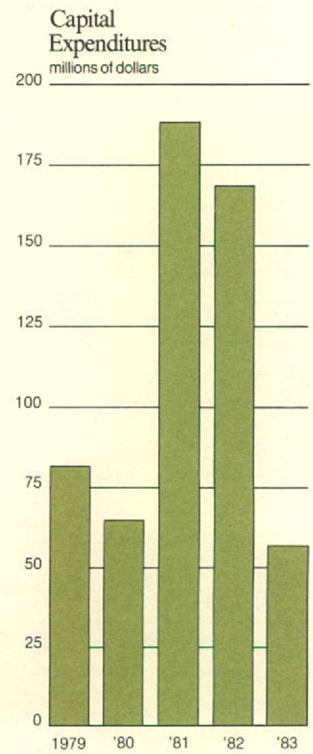
Except for per share amounts as indicated, all dollar figures are in thousands	1979	1980	1981	1982	1983
SALES & EARNINGS					
Net sales: pulp and paper	299,407	503,861	529,671	416,246	453,185
building products	38,668	35,418	38,923	21,608	41,796
total	338,075	539,279	568,594	437,854	494,981
Operating profit	108,410	174,210	159,930	57,203	35,429
Interest expense	10,944	8,893	8,154	6,630	17,679
Depreciation	20,203	28,375	30,603	33,701	39,863
Earnings (loss) before income taxes	81,603	143,105	130,421	17,350	(22,901)
Income taxes	35,008	61,753	49,400	(1,202)	(12,965)
Net earnings (loss)	46,595	81,352	81,021	18,552	(9,936)
Net earnings (loss) per share	12.44	18.01	16.59	3.80	(2.03)
Dividends declared, total	5,731	9,280	14,164	15,630	5,862
Dividends per share	1.50	2.00	2.90	3.20	1.20
ASSETS & LIABILITIES					
Current assets	109,524	222,455	143,295	151,762	141,796
Current liabilities	91,396	96,726	65,310	102,771	115,101
Ratio of above assets to liabilities	1.2	2.3	2.2	1.5	1.2
Working capital	18,128	125,729	77,985	48,991	26,695
Inventories, described in balance sheet	49,915	64,030	72,940	75,564	72,990
Fixed assets, see notes to financial statements	468,927	508,555	682,667	844,613	892,490
Accumulated depreciation	182,677	210,555	239,946	272,183	309,232
Long-term debt	76,767	70,948	75,597	154,021	171,862
Ratio of above debt to shareholders' equity	.5	.3	.2	.5	.5
Deferred income taxes	79,498	89,613	115,084	134,453	120,942
Retained earnings at year end	136,447	208,519	275,376	278,298	262,500
EQUITY & OTHER DATA					
Common shares outstanding at year end	3,907,484	4,884,355	4,884,355	4,884,355	4,884,355
Number of shareholders	2,557	2,726	2,518	2,397	2,080
Percentage of shares held in Canada	98.0	98.4	98.4	98.4	98.5
Shareholders' equity, total	148,113	263,168	330,025	332,947	317,149
Shareholders' equity per share	37.90	53.88	67.57	68.17	64.93
Cash flow from operations	84,891	119,842	137,095	71,622	16,416
Cash flow per share	22.66	26.53	28.07	14.66	3.36
Net earnings (loss) percentage on net sales	13.8	15.1	14.2	4.2	(2.0)
Annual expenditures on fixed assets	81,931	65,612	189,023	168,765	56,023
Number of employees on payroll	5,598	5,709	5,745	5,246	5,598

Net earnings per share and cash flow per share are based on the average number of shares outstanding during the year. Dividends per share are based on the number of shares outstanding at the record dates of the dividends. Certain figures for 1979 to 1981 on pages 22 and 23 have been restated from those originally reported to reflect retroactive application of the 1982 change in accounting for investment tax credits.









Results by Quarters

1983 Sales and Earnings
('000 omitted)

Quarter	Net Sales	Oper. Profit	Net Earnings (Loss)
First	$104,958	$ 4,558	$(7,721)
Second	129,723	10,699	(108)
Third	127,188	11,495	(352)
Fourth	133,112	8,677	(1,755)
	$494,981	$ 35,429	$(9,936)

Net Earnings (Loss) Per Share

Quarter	1979	1980	1981	1982	1983
First	$ 2.12	$ 5.09	$ 4.23	$ 2.95	$(1.58)
Second	2.79	4.42	4.44	1.56	(0.02)
Third	3.59	4.41	4.07	0.19	(0.07)
Fourth	3.94	4.09	3.85	(0.90)	(0.36)
	$12.44	$18.01	$16.59	$ 3.80	$(2.03)

Board of Directors at December 31, 1983

C. R. BOWLES *executive vice-president, Great Lakes Forest Products Limited*	Thunder Bay	1964
•R. W. CAMPBELL *vice-chairman and chief executive officer, Canadian Pacific Enterprises Limited*	Calgary	1983
•C. J. CARTER *chairman of the board and president, Great Lakes Forest Products Limited*	Thunder Bay	1947
R. E. CHAMBERS *executive vice-president, Great Lakes Forest Products Limited*	Thunder Bay	1959
R. S. DEMONE *president and chief operating officer, Maple Leaf Mills Limited*	Toronto	1981
†J. R. JONES *president, Lakehead Newsprint Limited*	Thunder Bay	1981
•W. NORMAN KISSICK *chairman and chief executive officer, Union Carbide Canada Limited*	Toronto	1982
†•RICHARD C. MEECH, Q.C. *partner, Borden & Elliot, barristers and solicitors*	Toronto	1980
•B. H. RIDDER, JR. *chairman of the executive committee, Knight-Ridder Newspapers, Inc.*	St. Paul, Minnesota	1957
THE HON. IAN D. SINCLAIR, O.C., Q.C., Senator *chairman, Canadian Pacific Enterprises Limited*	Toronto	1969
WILLIAM W. STINSON *president, Canadian Pacific Limited*	Montreal	1982
†G. GORDON STRONG *retired publisher*	Oakland, California	1968
J. G. TREZEVANT *senior vice-president, Field Newspaper Syndicate*	Irvine, California	1975
KENNETH A. WHITE *chairman, Commercial Union Holdings Limited*	Toronto	1977

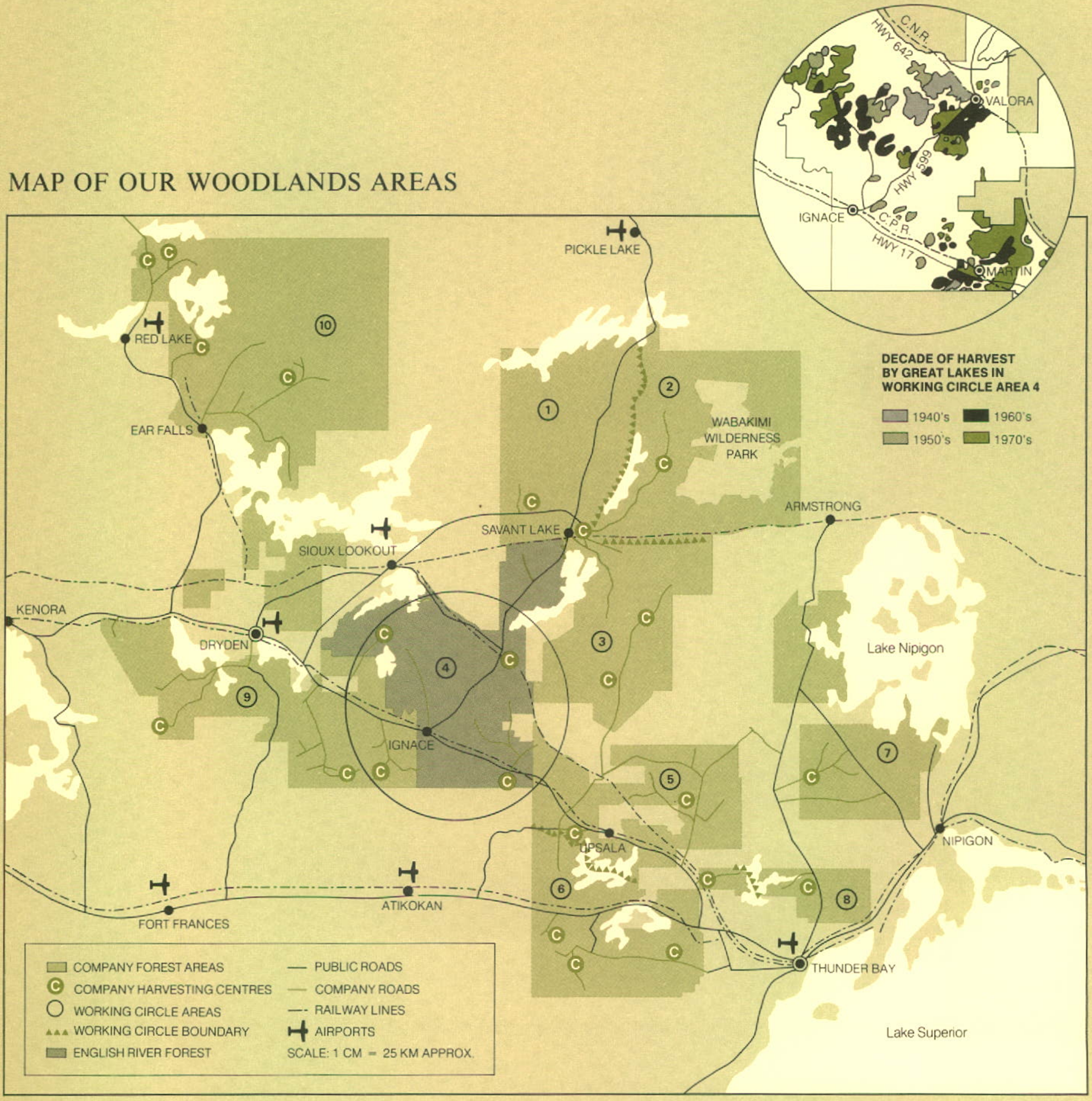
* *Members of the Executive Committee*
† *Members of the Audit Committee*
Years denote beginning of connection with the company or acquired operations.

Honorary director, R. G. MEECH, Q.C.

Management at December 31, 1983

C. J. CARTER, *chairman of the board and president*	1947
C. R. BOWLES, *executive vice-president*	1964
R. E. CHAMBERS, *executive vice-president*	1959
M. CEBROWSKI, *vice-president, mill operations*	1964
M. R. MCKAY, *vice-president, woodlands operations*	1944
K. E. WINROW, *vice-president finance and comptroller*	1971
T. M. BROWN, *secretary*	1956
D. D. MORROW, *treasurer*	1964
W. E. MACVITTIE, *assistant comptroller*	1968
R. A. LEHTOVAARA, *assistant comptroller*	1975
B. R. KERR, *assistant treasurer*	1964
F. H. TOLLEFSEN, *manager, public relations*	1966

MAP OF OUR WOODLANDS AREAS



The map shows our woodlands areas for both Thunder Bay and Dryden operations. These forest areas encompass some 21,000 square miles which are held under licence from the Province of Ontario. Also shown are the subdivisions into which the total forest area is divided for management purposes. Each numbered area is a separate forest management unit or working circle which has specified objectives for 20-year periods including the annual allowable harvest, regeneration guidelines and the road system. About 4,055 kilometres of company roads provide access to all our woodlands operations. Some working circles have an extensive road system as a result of development started in the 1930's, while others, such as areas 1, 2 and 10, have undergone later development as wood requirements increased due to recent mill expansions.

40-Year Harvest Pattern

The upper right circle which is taken from the English River Forest shows a typical harvesting pattern that has taken place over the past four decades. This activity will continue for another four decades in the white areas shown in the working circle at which time forests that were cut in the 1940's will be ready for a second harvest. For example, in the past few years we commenced cutting second-growth timber for our Dryden mill which started operations in the second decade of this century. The English River Forest shown on the map is the one area at present under a forest management agreement with the Province as discussed on page 6. Wabakimi Park which was created by the Ontario Government in 1983 and removed 629 square miles from our licensed area is also discussed on page 6. As well as roads and rail lines the map shows harvesting centres. Wood is brought from the forest areas to the mill by rail and truck on a scheduled delivery system.