Great Lakes Forest Products Limited Annual Report 1984

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 in 1980 the company undertook an 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 in April 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 paper used for 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 The St. Regis Group of Champion International 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
1980	$73.50	$44.00
1981	93.50	67.00
1982	81.50	46.00
1983	91.50	58.50
1984	91.00	76.00

Our Net Earnings and Dividends

Year	Net Earnings (Loss)	Dividends Declared
	per share	
1980	$18.01	$2.00
1981	16.59	2.90
1982	3.80	3.20
1983	(2.03)	1.20
1984	3.64	1.30

HIGHLIGHTS

'000 omitted	1984	1983
Net sales: Pulp and paper	$554,609	$453,185
Building products	47,367	41,796
Total	601,976	494,981
Operating profit	96,144	35,429
Earnings (loss) before income taxes	26,870	(22,901)
Income taxes	9,091	(12,965)
NET EARNINGS (LOSS): Total amount	17,779	(9,936)
Per share	3.64	(2.03)
Cash flow	71,448	16,416
Expenditures on fixed assets	47,223	56,023
Working capital at year end	74,859	26,695

Financial and five-year shipment summaries are shown on pages 20, 21 and 22.

- ☐ Net earnings were $17.8 million in 1984 compared with a loss of $9.9 million in 1983, the improvement mainly due to stronger markets for our major products.
- ☐ Record net sales of $602 million in 1984 versus $495 million in 1983 resulted from improved pulp and paper prices and higher shipments of all our products.
- ☐ Start-up of the Dryden fine paper machine in April marked the completion of the modernization and expansion program which commenced in 1980.
- ☐ In November we announced our intention to participate with five U.S. newspaper publishers in a joint venture to construct and operate a newsprint mill in Washington State.

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 bales of kraft pulp at our Dryden mill are shown in a pile of northern softwood jackpine chips. The chipping operation is the initial step in the pulp manufacturing process. In the next stage, wood chips are fed on a continuous basis to a 55-metre-high vessel known as a digester where chemicals combined with heat separate the cellulose fibres from the lignin, the binder in the wood. The fibres then enter the bleach plant where the remaining dark brown lignin is removed resulting in pure white fibres called bleached kraft pulp. The pulp is then dried, cut into sheets and baled. Noted for its strength and whiteness, kraft pulp manufactured at the Thunder Bay and Dryden mills owes its quality to up-to-date technology, the expertise of the operating personnel and the unique properties of the northern tree species. At our Thunder Bay mill we manufacture both softwood and hardwood kraft pulp. The various uses of kraft pulp are mentioned on the opposite page.

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 22, 1985.

TO THE SHAREHOLDERS

Improved economic conditions and stronger markets were largely responsible for a profit in 1984 compared with a loss the previous year. It is gratifying to report this improvement after the difficult period we have been through. I would like to extend sincere appreciation on behalf of the directors to all our employees for their full support in achieving these results.

The massive undertaking to modernize and expand our Dryden facilities which commenced in 1980 was completed in 1984 with the start-up of the fine paper machine early in the year. This $350 million program entailed replacing 80 percent of the kraft pulp mill, construction of a new stud lumber mill and the installation of a large fine paper machine, as well as construction of the necessary environmental facilities to meet government standards. We take pride in this accomplishment and congratulate all those who took part in this project. The official opening of the new Dryden facilities is shown in the photograph below.

In 1984 we announced our intention to participate in a new venture in the State of Washington as discussed on page 7. We believe this is a promising opportunity that augurs well for the future of our company.

We were sorry to lose three directors who retired in 1984 after serving with distinction for many years: G. Gordon Strong, formerly president, Oakland Tribune Inc.; The Hon. Ian D. Sinclair, O.C., Q.C., Senator, formerly chairman, Canadian Pacific Enterprises Limited and Kenneth A. White, formerly chairman, Royal Trustco Limited. Mr. Strong joined the Board in 1968, Senator Sinclair in 1969 and Mr. White in 1977. The directors expressed their gratitude to the retiring directors for their valuable contribution to the progress of our company.

We welcomed three new directors: J. Ross LeMesurier, retired investment dealer, Toronto; Bartlett B. Rombough, president and chief executive officer, PanCanadian Petroleum Limited, Calgary and Stanley H. Stauffer, president, Stauffer Communications Inc., Topeka, Kansas, who were elected to the Board at the shareholders' meeting.

On behalf of the directors,

CHARLES J. CARTER,
chairman and president

Thunder Bay, Ontario
January 31, 1985

Senator Ian D. Sinclair, former chairman, Canadian Pacific Enterprises Limited and a retired director of our company, cuts the ribbon officially opening our modernized and expanded mill facilities in Dryden, July 25, 1984. Holding the ribbon on the left is Wayne Wolfe, resident manager of the Dryden mill and Lorne Crawford, resident manager of the Dryden woodlands operations. In the background is the name plate for the fine paper machine.

IMPROVED RESULTS IN 1984; RECORD SALES, SHIPMENTS UP

Net earnings for 1984 were $17.8 million or $3.64 per share compared with a loss of $9.9 million or $2.03 per share in 1983. Higher shipments of all products, improved prices for pulp and paper products and higher exchange premium on U.S. dollar sales were the major factors in this turnaround. Cost inflation in energy, transportation, labor and chemicals continued in 1984, although at a more moderate rate than in previous years. Interest and depreciation charges increased with the commencement of operations of the new Dryden fine paper machine in the second quarter.

Record Sales

Net sales were $602 million in 1984 versus $495 million in 1983. Shipments of all products increased in the year.

Demand for kraft pulp improved in the first half of 1984 and increased prices prevailed until late in the year when a softening market resulted in some erosion of the earlier price increases. The average price of kraft pulp in 1984 was equivalent to 1980 prices. We maintained essentially full operations throughout the year and shipments of kraft pulp increased due to improved operating performance of the Dryden mill in comparison with the breaking-in period of the previous year.

In 1984 newsprint markets strengthened allowing for a modest price increase by mid-year. This was the first time that newsprint prices exceeded levels established in 1981. Full operations were maintained during the year and higher newsprint shipments reflect improved operating performance.

Price increases for fine papers went into effect in the first half of 1984 as the market improved. However, a softening of markets late in the year resulted in some price deterioration. Increased shipments of fine papers reflect increased capacity with the start-up of the new fine paper machine in Dryden on April 4 replacing the three old fine paper machines.

The building products market showed some signs of improvement early in the year but for most of 1984 depressed markets prevailed. Although prices for stud lumber continued to deteriorate throughout the year, waferboard prices improved slightly in the last two months of 1984. Increased shipments of stud lumber reflect a full year of operation of the stud lumber mill in Dryden compared with only half a year of production in 1983 following the May start-up of this new facility and phasing out of the old dimension lumber mill. Waferboard shipments were also higher than in the previous year due to full operation in 1984 whereas the facility was shut down during the first six weeks of 1983.

Exchange Impact

Our average exchange premium on U.S. dollars was 21.7 percent in 1984, up from 18.7 percent in the previous year. Forward exchange contracts entered into in 1981 and completed in 1984 protected the value of a substantial portion of our U.S. dollar revenue during the period of major capital expenditures to modernize the Dryden facilities. These contracts, which were at an average premium of 17.4 percent in 1984 and covered 72 percent of our U.S. dollar sales, were a significant factor in determining our average exchange premium.

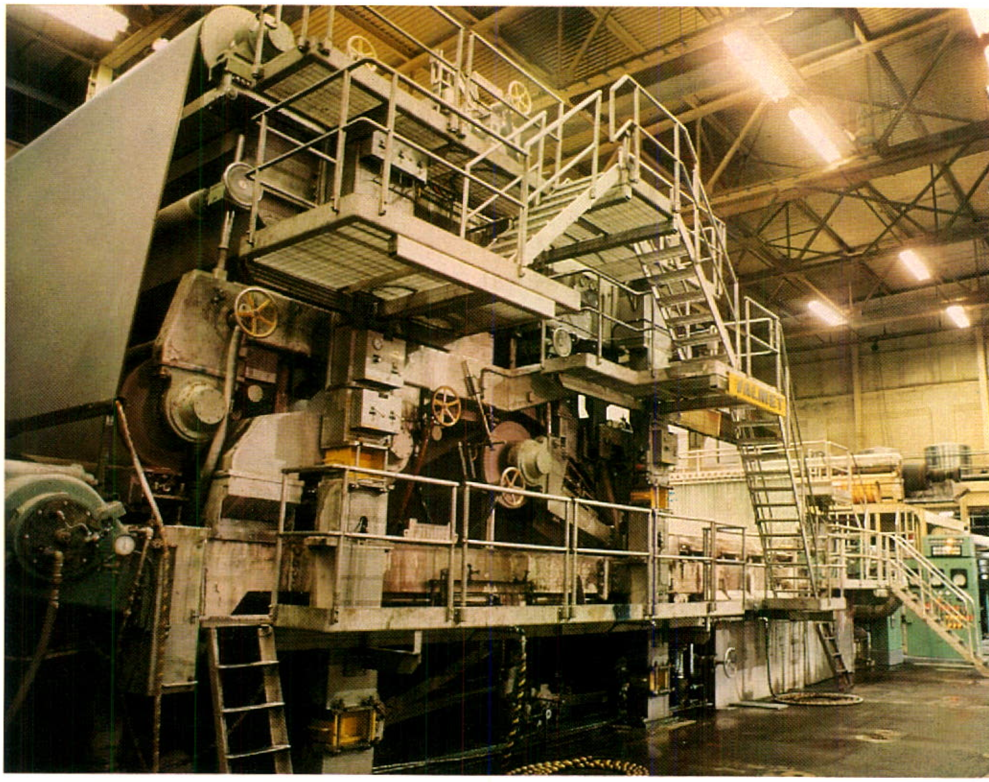
Income Taxes

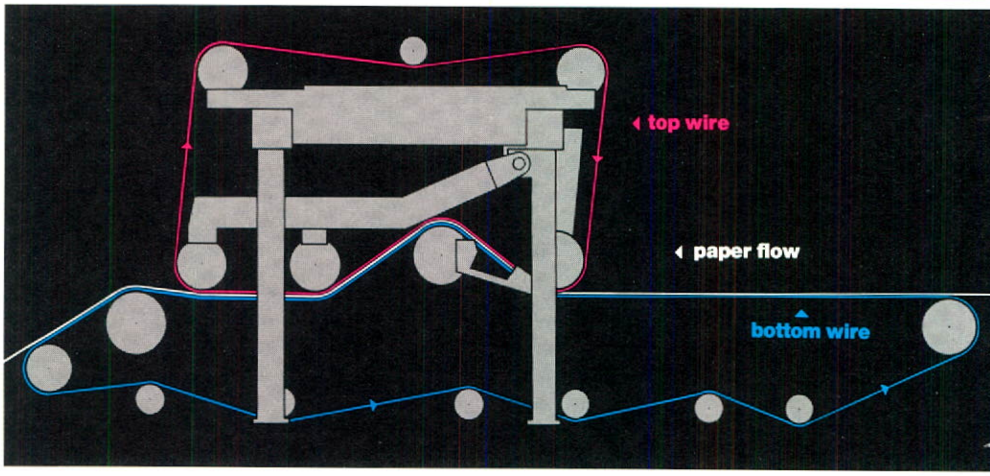
Income taxes were $9.1 million in 1984 compared with a tax recovery of $13 million on the loss in 1983. In both cases, the basic tax rate was approximately 45 percent but the lower effective rate of tax of 33.8 percent in 1984 and the higher effective rate of recovery of 56.6 percent in 1983 were largely the result of investment tax credits. Due to the accelerated tax write-offs from the high level of capital expenditures in recent years, substantially all of the 1984 taxes have been deferred.

Dividends

Dividends of $1.30 per share were declared in 1984 compared with $1.20 per share in 1983. The directors

Tilling or scarifying the soil on a cutover forest site in preparation for planting or seeding is a key step in the regeneration process. The above powered-head scarifier, designed and developed by our woodlands personnel and Northern Engineering & Supply Co. Ltd. of Thunder Bay, is proving adaptable to the rugged terrain of Northwestern Ontario and provides higher productivity than other types of scarifying equipment.





To meet the changing demands of the marketplace we installed a Valmet top-wire former on No. 3 newsprint machine in 1984, shown above, which enhances the printing quality of our newsprint sheet. We plan to install a similar top-wire former on No. 4 machine in 1985. These major improvements to our manufacturing process enable our company to remain competitive with others in the industry using the newest machines.

increased the quarterly dividend rate on October 26 from 30 cents to 40 cents per share for the dividend payable January 2, 1985.

Capital Expenditures

In 1984 capital expenditures totalled $47.2 million. In Dryden $13.8 million was spent to complete the new 123,000-metric-ton-per-year fine paper machine which started up April 4. The Dryden modernization and expansion program which commenced in 1980 involves, as the final phase, the construction of some additional support facilities and the demolition of the old mill. In 1984 $5.5 million was spent on this phase with the work scheduled for completion in 1985. Other projects in Dryden included the upgrading of bark burning capabilities for the generation of steam.

Capital expenditure projects in the Thunder Bay mill operations included the installation of the top-wire former on No. 3 paper machine shown on page 4 and the new roll-tracking and order-entry system for our newsprint operation shown on page 6.

Woodlands capital expenditures in the Thunder Bay and Dryden operations were primarily for woodlands equipment and the extension of our road network.

Our Forest Resources

The Ontario Ministry of Natural Resources program of forest management agreements, known as FMA's, gives the company responsibility for planning and implementing a complete forest management program including harvesting, road construction and regeneration of cutover areas.

The English River Forest Management Agreement, our first FMA, is in its fifth year. This area is one of ten which comprise our total forest area as shown on the map on page 23. Since the signing of the FMA in the spring of 1980 forest management activities conducted on the English River Forest include the following harvesting and regeneration work:

- —50,700 acres harvested
- —5,270 acres planted with 3,200,000 trees
- —51,400 acres seeded, most of which received prior site preparation treatment
- —1,770 acres prepared for natural seeding
- —1,160 acres prescribed for natural regeneration

The total cutover area treated of 59,600 acres includes some areas that were harvested prior to 1980. In addition 2,120 acres of conifer regeneration were tended with herbicide to control competing vegetation. It should be noted that the Ministry was responsible for the regeneration work in 1980, the phasing-in period of this FMA. Our first five years of stewardship under this agreement will be audited in 1985.

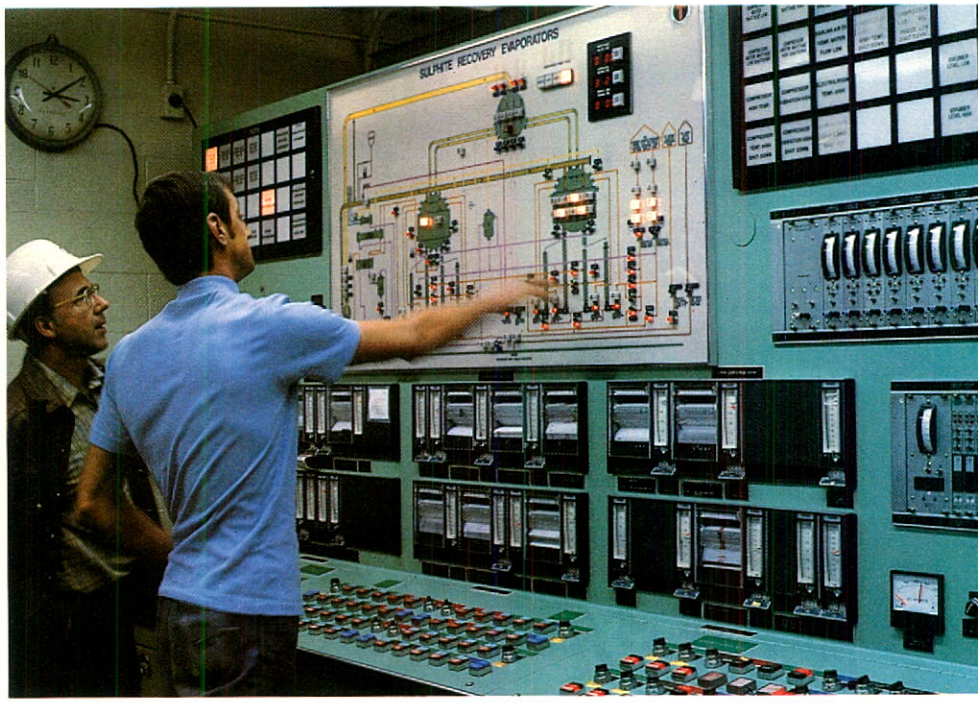
In September 1984 we signed a second FMA with the Ontario Government which covers the Trout Lake Forest, an area of some 3,800 square miles north of Dryden and is a major source of wood supply for our Dryden mill operations. Two more FMA's in our Thunder Bay operating area, one covering working circle 3 and the other for working circles 5 and 6 combined, as shown on the woodlands map, are expected to be signed early in 1985.

Extensive spruce budworm infestation on approximately half our woodlands areas north and west of Thunder Bay has been a cause of grave concern in the past year. The spruce budworm spray program which had been announced by the Ministry for infested forestland within our woodlands areas was cancelled for the 1984 season. Almost 14 million acres of forest throughout Northwestern Ontario have been damaged by the spruce budworm with balsam fir and spruce trees suffering moderate to severe defoliation and large areas of trees left dead or dying. Unless something is done to arrest this infestation it could have serious implications for our long-term wood supply. Consequently, we continue to press the Ministry to implement an effective control program.

The Ontario Tree Improvement Council was formed in 1984. Through our company participation on this council, which includes members from the Ministry and the forest industry of Ontario, we will be able to participate directly in the development of genetic improvements to planting stock and tree seeds for our regeneration programs.

The above checker in our shipping department is using a sensor to "read" a shipping ticket carrying a bar code similar to the familiar bar code that appears on all kinds of merchandise. The ticket has been removed from the newsprint roll shipping label and the information on the ticket, which includes roll number and size, is automatically fed to a computer where these facts are checked against the customer's original order. The system is used to check all rolls in each rail car or van before they leave the mill. As well as improving the service to customers, this new roll-tracking and order-entry system provides major efficiencies in our shipping operation.

In the cross-recovery system in Thunder Bay, which is controlled from the panel shown on the upper right, spent sulphite chemicals are reduced to a concentrated form, then transferred from the high-yield sulphite pulp operation in the newsprint mill to the chemical recovery furnace in the kraft pulp mill. The first of its kind in North America, the system provides a major advance in further reducing oxygen-consuming wastes in the liquid discharge from the mill to meet government environmental requirements.



The new 5.5-metre-wide fine paper machine in Dryden, above, which started up in April 1984, is capable of producing 123,000 metric tons annually of printing, envelope and specialty papers. This world-class machine greatly enhances our position in Canadian and U.S. markets for fine paper products. The machine is called "Patricia" after the region in which Dryden is located.

Employee Relations

In 1984 three-year agreements were signed with all unions representing our employees extending to various expiry dates between April 30 and September 30, 1987. These agreements provide for wage increases in line with those negotiated throughout the industry in Eastern Canada. Substantial improvements were made to the mill employees' pension plans similar to those previously granted by other major Ontario forest products producers. The principal improvement provides retiring employees with pensions based on their final five years' earnings compared to career average earnings under the previous plans. A pension plan was introduced for woodlands employees that provides benefits based on defined contributions by the company. Previously, the woodlands employees did not have a pension plan.

Washington State Venture

On November 28 we announced our intention to participate with five U.S. newspaper publishers in a joint venture to construct and operate a 154,000-metric-ton-per-year newsprint mill in Northeastern Washington State.

The facility would be owned and operated by a partnership, to be known as Ponderay Newsprint Company, with 40 percent participation by a wholly-owned U.S. subsidiary of our company. This subsidiary would act as the managing partner responsible for construction and operation of the mill. The five newspaper publishers, who would collectively represent the remaining 60 percent participation, would enter into firm contracts to purchase more than 80 percent of the total mill output and the balance would be sold on the open market.

The project, which still requires satisfactory arrangements for electrical power supply, clearance by environmental and other authorities and financing, could be completed by mid-1987.

Estimated development and construction costs for the project would be in excess of $210 million (U.S. funds) excluding financing costs and working capital. Financing has not been completed but it is expected that it would be structured on a project financed basis. Our investment in this project would total approximately $25 million (U.S. funds) over the two-year construction period.

The manufacturing facilities would include a thermomechanical pulping process and a 440-metric-ton-per-day twin-wire newsprint machine. The mill would use purchased wood chips from sawmills and chip producers in the area.

Market Outlook

Compared with the strong growth in 1984, the U.S. economy is expected to make more moderate gains in 1985. Such gains will provide a positive influence on our markets in the face of certain negative factors discussed below. Over the next few years the U.S. economy is expected to experience gradual growth, however, there are uncertainties that cloud the longer term outlook.

Oversupply, marked by high inventories and intense price competition, is the dominant factor affecting the kraft pulp market at the beginning of 1985 and this condition is expected to continue for at least the first half of the year. Major increases in world manufacturing capacity came on stream in 1984, but significantly less will be introduced in 1985 and 1986. Currently the strength of North American currencies provides a competitive disadvantage for Canadian and U.S. producers. Over the next few years, growth in demand for kraft pulp can be expected to absorb the increase in supply bringing a return to more stable market conditions. Over the longer term, with market opportunities in the Far East and elsewhere and anticipated growth in the numerous paper products using kraft pulp as a prime ingredient, we believe there is a rewarding future for this product.

U.S. newsprint consumption was 11.4 million metric tons in 1984, up 7.5 percent over 10.6 million metric tons in 1983. It is expected that, with the projected moderate growth in the U.S. economy, consumption will continue to increase in 1985 but at a slower rate. We expect to see increased competition from offshore producers who currently enjoy the advantage of strong North American currencies. However, on balance, we believe that the U.S. newsprint market will remain fairly stable over the next year or so with little new manufacturing capacity coming on line. Looking ahead, we expect a general upward trend in newsprint demand and believe the prospects for this product are encouraging.

Fine papers are expected to undergo slower growth in 1985 compared with the previous year. The oversupply situation which developed late in 1984 is expected to result in a softer market during 1985 with a dampening effect on prices. We believe that there will be a gradual improvement in the fine paper market over the next few years as economic conditions improve and supply and demand return to a better balance. Looking to the future, we are optimistic that demand for this product will continue to grow, affected from time to time by the cyclical fluctuations we have experienced in the past.

North American housing starts are expected to be moderately lower than 1984 and oversupply of waferboard and softwood lumber will continue to undermine the market in 1985. However, stud lumber is expected to outperform random length lumber and it is anticipated that waferboard will continue to gain an increased share of the panelboard market. Current proposals in the United States to establish import quotas on Canadian lumber could seriously affect Canadian shipments to that country. Over the longer term, we expect to see a steady market for building products which will be served by the most cost-efficient producers.

Company Outlook

We look for improved earnings in 1985 over the previous year with a high level of operations despite softness in some of our markets and continued intense price competition. A significant factor in this improvement is the higher U.S. dollar exchange premium which we expect to experience.

Over the next few years, we expect gradual improvement in our markets although anticipated slower economic growth and uncertainty dampens the outlook for an early return to the buoyant markets of the early 1980's. With our modern expanded facilities in Dryden now in full operation and the efficiency of our Thunder Bay facilities which have been updated and improved over the years, as well as our highly mechanized woodlands operation and, most important, our skilled work force, we believe we can hold our own in the face of the ever-growing competitive challenge in the international markets for our products.

It has always been our policy to seek opportunities for growth and, when appropriate, we have been ready to entertain any move that will advance our company. We believe that our proposed venture in Washington State presents an excellent opportunity to expand our horizons. Such diversification of our operations can be expected to increase our strength and stability and improve the flexibility of our marketing efforts.

Looking at the long term, we are optimistic that our markets will continue to grow notwithstanding the temporary setbacks which our industry experiences from time to time. We are confident that we can take advantage of the anticipated growth and maintain our fair share of the markets we serve. We further believe our enterprise is strong and will serve us well in good times and bad as we move into the future providing well-earned benefits to all those who have given us their support over the years.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF 1984 FINANCIAL STATEMENTS

Operating Results

Net sales of $602 million in 1984 increased $107 million or 21.6 percent over the prior year. Higher shipment volumes for all products contributed $37.7 million to this increase and improved net selling prices for newsprint, kraft pulp and fine papers provided the remaining $69.3 million. The higher shipment volumes in 1984 reflect improved performance in newsprint and kraft pulp operations and increased fine paper and stud lumber production capacities from new facilities in Dryden. Improved waferboard shipments reflect a full year's operation in 1984 whereas in 1983, the plant was shut down until mid-February.

Improved markets for newsprint in 1984 resulted in a modest price increase mid-year. This was the first time newsprint prices rose above their mid-1981 level. Strengthening of kraft pulp markets also resulted in price increases through the first three quarters of 1984. However, growing competition in North American pulp markets in the last quarter, notably from offshore suppliers to whom the strong performance of the U.S. dollar was a factor, reversed some of the earlier gains. Kraft pulp prices for 1984 averaged approximately their 1980 levels. Fine paper markets strengthened throughout most of 1984 but stiffer competition in the latter part of the year resulted in some erosion of prices by year end. Stud lumber and waferboard prices remained weak in 1984. While average prices for these products were lower during the year, a slight recovery of waferboard prices occurred in the fourth quarter.

Forward exchange contracts, which were completed at the end of 1984, were negotiated in 1981 to protect the value of a significant portion of the company's U.S. dollar revenue which was being relied upon to finance a major portion of the heavy capital spending on the Dryden modernization program. The contracts covered 72 percent of U.S. dollar sales proceeds in 1984 compared to 78 percent in 1983. The exchange premium on U.S. dollar sales proceeds, which was largely determined by the forward contracts, averaged 21.7 percent in 1984 compared with 18.7 percent in 1983.

Cost of sales of $493.9 million increased $47.4 million in 1984 primarily due to higher shipment volumes of kraft pulp, fine papers and stud lumber from our Dryden facilities. The new fine paper machine started up successfully in April providing more efficient operation and increased capacity. All other manufacturing facilities operated at virtually full capacity throughout the year. Steady improvement in the operating performance of the kraft pulp and stud lumber mills in Dryden combined with the higher volumes from the new fine paper machine have partially offset continued escalation of manufacturing costs as a result of inflation. Selling and administrative expenses of $11.9 million in 1984 were $1.1 million lower than the prior year due largely to lower selling costs.

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

Interest costs rose $4.1 million to $27.2 million in 1984 due to higher levels of borrowings. Interest charged to earnings was $24.8 million in the year compared to $17.7 million in 1983 and interest capitalized in connection with construction of the new fine paper machine was $2.4 million in 1984 compared with $5.4 million in 1983.

A charge of $2 million in 1984 for exchange on foreign currency debt reflects the conversion of U.S. dollar debt to current exchange rates and the amortization of unrealized exchange losses on long-term debt as explained below. Depreciation expense of $43.9 million increased by $4 million in 1984 due largely to the additional depreciation associated with the new fine paper machine. Income taxes of $9.1 million on pre-tax earnings of $26.9 million in 1984 compare with tax recoveries of $13 million on a pre-tax loss of $22.9 million in 1983. The basic tax calculation in both years was at a rate of approximately 45 percent. However, the lower effective tax rate in 1984 of 33.8 percent and the higher effective rate of tax recovery in 1983 of 56.6 percent were largely due to investment tax credits earned in the respective years.

The company has adopted new recommendations of the Canadian Institute of Chartered Accountants on foreign currency translation which have been applied effective January 1, 1984. The principal change affecting the company is the requirement to translate all debt payable in foreign currency, regardless of maturity, at the exchange rate in effect at the balance sheet date. Any unrealized exchange gain or loss on long-term debt is deferred and amortized over the remaining life of the debt. The effect of this change has been to reduce net earnings for 1984 by $981,000 or 20 cents per share.

Financial Condition

Working capital increased substantially in 1984 to $74.9 million from $26.7 million at the end of 1983. The principal changes within working capital were: an increase of $12.7 million in accounts receivable due to the higher selling prices and exchange rates at the end of 1984, an increase of $20.6 million in inventories due largely to higher quantities of wood and materials and supplies on hand at the end of the year to meet operational requirements, and a reduction of $14.6 million in the current portion of long-term debt as a result of the repayment at maturity of the 8¾ percent debentures in early 1984. Cash flow from operations in 1984 was $71.4 million compared to $16.4 million in 1983. This improvement was largely the result of improved earnings and the deferral of a substantial portion of income taxes.

Three-year labor agreements were negotiated in 1984 with all unions representing our employees providing wage increases in line with those negotiated throughout the industry in Eastern Canada. The company granted improvements in the mill employees' pension plans similar to those previously granted by other major Ontario forest products producers. The principal improvement provides retiring employees with pensions based on their final five years' earnings compared to career average earnings under the previous plans. These improvements, which are being funded over 15 years, substantially increase the liability for past service and are the main reason for the increase in the estimated unfunded amount from $10 million at the end of 1983 to $50.7 million at the end of 1984. The company also introduced a pension plan for woodlands employees that provides benefits based on defined contributions by the company. The woodlands employees did not previously have a pension plan.

Capital expenditures amounted to $47.2 million in 1984. Expenditures on the major Dryden capital program were $13.8 million for completion of the fine paper machine and $5.5 million for construction of support facilities and demolition of parts of the old kraft pulp mill. Other projects in the Dryden mill amounted to $3.5 million including the upgrading of bark-burning capabilities for the generation of steam. Thunder Bay mill expenditures totalled $18.3 million including a top-wire former for one of the newsprint machines. Woodlands expenditures were $6.1 million for equipment replacement and road construction.

In 1984 the company renegotiated its loan agreements with two Canadian banks to provide unsecured operating lines of credit of $50 million each, in either Canadian or U.S. funds, at floating rates. Previously these agreements were secured by accounts receivable and inventories. During the year the company drew down an additional $35 million under its various line-of-credit agreements.

As at December 31, 1984, the relationship of debt to debt plus equity increased to 42.8 percent from 41.6 percent in 1983 and floating rate borrowings represented 67.2 percent of total debt compared to 66 percent at the end of 1983.

Effects of Economic Conditions

Net earnings for 1984 were $17.8 million compared to a loss of $9.9 million in 1983. The improvement in results was largely due to higher average prices for newsprint, kraft pulp and fine papers reflecting stronger markets for these products for most of the year. Continued recovery at a modest pace is forecast for 1985. Newsprint is expected to continue strengthening. Pulp markets, which weakened during the last quarter of 1984, will continue to show softness for at least the first half of 1985. Fine paper markets will be keenly competitive in 1985 but we expect some strengthening late in the year. Markets for building products are not expected to improve in 1985 due to continued excess production capacity. U.S. dollar exchange premium is expected to provide substantial improvement in earnings in 1985 following completion of the forward exchange contracts. The company continues to emphasize the importance of cost control through the rationalization of employment levels, production process improvements and energy conservation measures. In addition, capital expenditure proposals continue to be closely scrutinized. The completion of the $350 million Dryden modernization and expansion program provides the company with new efficient facilities for the production of kraft pulp, fine papers and stud lumber. These facilities have provided increased capacities with reduced manpower requirements and are expected to continue to contribute toward improved results. The proposed joint venture with five U.S. newspaper publishers for the construction and operation of a newsprint mill in Northeastern Washington State will provide an opportunity to further strengthen our earnings potential in the years ahead.

Inflation Accounting

The Canadian Institute of Chartered Accountants recommends the reporting of certain supplementary information on the effects of changing prices. These recommendations were not widely adopted in Canadian financial reporting in 1983. The company has expressed reservations in previous annual reports and continues to be concerned about the subjective nature of this information, the difficulty in interpreting its significance and its lack of general usefulness to the readers of our financial statements in assessing the performance or future prospects of this company. For these reasons, the supplementary information has not been reported.

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, 1984 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, 1984 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, except for the change in the method of accounting for foreign currency translation as explained in Note 4 to the financial statements, on a basis consistent with that of the preceding year.

Thorne Riddell

Toronto, Canada, January 20, 1985

THORNE RIDDELL
Chartered Accountants

EARNINGS

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

	1984	1983
Net sales:		
Pulp and paper	$554,609	$453,185
Building products	47,367	41,796
	601,976	494,981
Cost of sales	493,927	446,511
Selling and administrative expense	11,905	13,041
OPERATING PROFIT	96,144	35,429
Interest and other income	1,341	1,484
	97,485	36,913
Interest (Note 6)	24,789	17,679
Exchange on foreign currency debt (Note 4)	1,974	2,272
Depreciation	43,852	39,863
EARNINGS (LOSS) before income taxes	26,870	(22,901)
Income taxes (Note 7)	9,091	(12,965)
NET EARNINGS (LOSS)	$ 17,779	$ (9,936)
Net earnings (loss) per share	$ 3.64	$ (2.03)

RETAINED EARNINGS

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

	1984	1983
Retained earnings at beginning of year	$262,500	$278,298
Net earnings (loss)	17,779	(9,936)
	280,279	268,362
Dividends declared	6,350	5,862
RETAINED EARNINGS at end of year	$273,929	$262,500

BALANCE SHEET

consolidated statement at December 31 (thousands of dollars)

	1984	1983
Assets		
CURRENT ASSETS		
Cash	$ 2,229	$ 121
Accounts receivable	79,607	66,867
Inventories:		
Finished goods	13,371	8,942
Pulpwood and sawlogs	44,699	34,968
Materials and supplies	35,483	29,080
Prepaid expenses	2,502	1,818
	177,891	141,796
FIXED ASSETS (Note 2)	937,689	892,490
Accumulated depreciation	351,443	309,232
	586,246	583,258
DEFERRED FOREIGN EXCHANGE (Note 4)	4,092	–
	$768,229	$725,054

	1984	1983
Liabilities		
CURRENT LIABILITIES		
Accounts payable and accrued charges	$ 52,635	$ 51,080
Loan payable (Note 10)	37,705	38,000
Income and other taxes payable	9,566	8,789
Dividend payable	1,954	1,465
Current portion of long-term debt	1,172	15,767
	103,032	115,101
LONG-TERM DEBT (Note 3)		
First Mortgage Bonds:		
8% sinking fund bonds, Series B, maturing 1989	9,830	10,002
11¼% sinking fund bonds, Series C, maturing 1995	28,002	29,264
8¾% debentures maturing 1984	—	12,143
Term loan (U.S. $25 million)	33,042	30,860
Notes payable	8,554	11,430
Lease obligations	1,277	2,497
Bank loans	127,308	89,161
	208,013	185,357
Current portion	1,172	13,495
	206,841	171,862
DEFERRED INCOME TAXES	129,778	120,942
Shareholders' Equity		
Common shares (4,884,355 shares issued)	54,649	54,649
Retained earnings	273,929	262,500
	328,578	317,149
	$768,229	$725,054

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)

	1984	1983
WORKING CAPITAL PROVIDED		
Net earnings (loss)	$ 17,779	$ (9,936)
Items not affecting working capital:		
Depreciation	43,852	39,863
Deferred income taxes	8,836	(13,511)
Amortization of deferred foreign exchange (Note 4)	981	–
GENERATED FROM OPERATIONS	71,448	16,416
Government grants	–	4,693
Issue of long-term debt	35,256	35,877
Sale of fixed assets	383	639
	107,087	57,625
WORKING CAPITAL USED		
Expenditures on fixed assets	47,223	56,023
Reduction of long-term debt	5,350	18,036
Dividends declared	6,350	5,862
	58,923	79,921
INCREASE (DECREASE) IN WORKING CAPITAL	48,164	(22,296)
Working capital at beginning of year	26,695	48,991
WORKING CAPITAL at end of year	$ 74,859	$ 26,695

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Year ended December 31, 1984

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

Monetary assets and liabilities in foreign currencies are translated into Canadian dollars at rates of exchange at the date of the balance sheet with any unrealized exchange gain or loss on long-term debt deferred and amortized over the remaining life of the debt. Other assets and liabilities and items affecting earnings are converted at rates of exchange in effect at the dates of the transactions. In all cases, however, items covered by forward exchange contracts are converted at the contract rates.

Inventories

Inventories of finished goods are valued at the lower of average cost and net realizable value. Inventories of pulpwood and sawlogs and materials and supplies 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. The following methods and composite rates of depreciation are used for the principal assets of the business:

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, 1984		December 31, 1983
	Cost	Net Value	Net Value
Land	$ 1,485	$ 1,485	$ 1,495
Buildings, machinery and equipment			
Pulp and paper	778,596	530,002	433,015
Building products	45,881	18,049	21,961
Woodlands improvements and equipment	88,941	20,726	21,017
Timber licences	3,945	–	–
Assets under capital lease	3,065	208	1,034
Construction in progress	15,776	15,776	104,736
	$937,689	$586,246	$583,258

3. Long-Term Debt

The company has an unsecured term loan from a foreign bank in the amount of $25 million in 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 9 percent to 11 percent with expiry dates extending to 1989.

Loan agreements with two Canadian banks provide for unsecured operating lines of credit of $50 million each in either Canadian or U.S. funds at floating rates. These agreements continue to January 1, 1987 and June 1, 1987, respectively, with extensions thereafter at the discretion of the company subject to the right of the banks to refuse further extensions upon the giving of specified notice. As at December 31, 1984, $59 million in Canadian funds was owing under these agreements.

In addition, the company has loan agreements with two other banks for unsecured operating lines of credit of $50 million each in U.S. funds, or the 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, 1984, $51.3 million in U.S. funds was owing under these agreements.

Required amounts to reduce long-term debt over the next five years, based on the exchange rate at which the debt is recorded on the financial statements and assuming no extensions to existing bank loan agreements, are as follows (thousands of dollars):

	Bonds and Debentures	Bank Loans	Other	Total
1985	$ 710	$ –	$ 462	$ 1,172
1986	2,562	6,781	542	9,885
1987	2,870	75,296	3,013	81,179
1988	3,150	18,038	2,998	24,186
1989	6,860	18,038	3,048	27,946

4. Change in Accounting Policy

Effective January 1, 1984, the company has adopted the new recommendations of the Canadian Institute of Chartered Accountants on foreign currency translation as described in Note 1. The principal change affecting the company is the requirement to translate all debt payable in foreign currency, regardless of maturity, at the exchange rate in effect at the balance sheet date. The effect of this change has been to reduce net earnings for 1984 by $981,000 or 20 cents per share.

5. 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.

6. Interest

Interest for the year amounted to $22.4 million ($19.2 million in 1983) on long-term debt and $4.8 million ($3.9 million in 1983) on short-term indebtedness. Of these amounts, $2.4 million ($5.4 million in 1983) has been capitalized.

7. Income Taxes

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

	1984	1983
	thousands of dollars	
Earnings (loss) before income taxes	$26,870	$(22,901)
	percent	
Combined basic federal and provincial rate	51.0 %	
Manufacturing and processing allowance	(5.9)	
	45.1	
Deferred tax drawdown rate	–	(45.4) %
3% inventory allowance	(2.2)	(2.8)
Federal investment tax credits	(8.6)	(12.4)
Other	(0.5)	4.0
Effective rate of income tax (recovery)	33.8 %	(56.6) %

8. 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, 1984 and after giving effect to increases in benefits granted in 1984, the unfunded amount as at December 31, 1984 is estimated to be $50.7 million.

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". These expenditure requirements have been met by the company. 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 the 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, 1984, $21 million in Canadian funds and $12.6 million in U.S. funds was owing under this line of credit and interest for the year amounted to $4.8 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 1984, 87 percent (86 percent in 1983) of the company's net sales were exported, largely to United States destinations, and priced in U.S. dollars.

Industry Reference Data

NEWSPRINT PAPER

The United States is Canada's principal customer for newsprint and accounts for approximately 47 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 1980 through 1984. World totals for newsprint omit communist countries for which reliable information is lacking.

	1980	1981	1982	1983	1984
	(millions of metric tons)				
Free-world production capacity	24.9	26.0	27.3	27.9	28.2
Free-world production	23.0	24.1	22.5	23.4	25.0
Canadian production capacity	9.1	9.5	9.9	10.0	9.9
Canadian production	8.6	8.9	8.1	8.5	8.9
Canadian exports	7.6	7.9	7.1	7.5	7.9
Canadian exports to United States	6.1	6.1	5.6	6.0	6.5
Total U.S. consumption	10.1	10.2	10.1	10.6	11.4

Source: CPPA (1984 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 1984 of approximately 65.9 million metric tons or 65.1 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 1984 the production capacity in North America and Scandinavia for market bleached kraft pulp was approximately 16.1 million metric tons of which Canadian production capacity amounted to approximately 41.2 percent, or 6.6 million metric tons. Our company is a major supplier of this market pulp.

	1980	1981	1982	1983	1984
	(millions of metric tons)				
Paper Grade Chemical Pulp					
North American and Scandinavian production	59.4	59.9	55.2	60.3	63.2
Bleached Kraft Pulp					
North American and Scandinavian production	31.0	31.7	30.4	33.4	35.2
Market Bleached Kraft Pulp					
Total demand for North American and Scandinavian production	13.3	13.0	11.8	14.1	14.3
Canadian shipments	5.9	5.5	4.7	5.8	5.8
Canadian exports to United States	2.0	1.9	1.6	2.0	2.2
Total U.S. supply (including imports)	4.0	3.9	3.6	4.4	4.8

Source: CPPA (1984 estimated).

FINE PAPERS

The term "fine papers" 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 38 percent of all fine papers produced in Canada; printing grades, representing 43 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 19 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.

	1980	1981	1982	1983	1984
			(thousands of metric tons)		
Canadian production capacity	982.0	1,019.0	1,008.0	1,026.0	1,116.0
Domestic shipments	697.2	661.6	648.8	718.8	769.1
Export shipments	200.8	127.2	174.1	238.4	252.2
Canadian imports	150.9	217.7	153.3	195.9	270.0
Canadian demand	848.1	879.3	802.1	914.7	1,039.1

Sources: Statistics Canada, CPPA (1984 estimated).

LUMBER

Residential construction provides the principal use for softwood lumber produced in Canada and the United States, 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.

	1980	1981	1982	1983	1984
			(millions)		
North American housing starts	1.5	1.3	1.2	1.9	1.9
Seasonally adjusted year-end rate of North American housing starts	1.7	1.1	1.4	1.8	1.7
Softwood lumber production			(billions of board feet)		
United States	31.6	22.8	21.0	29.8	31.5
British Columbia	12.0	10.4	10.1	12.2	12.4
Rest of Canada	6.2	6.0	5.4	6.9	7.2
Total	49.8	39.2	36.5	48.9	51.1

Sources: Statistics Canada, U.S. Bureau of Census, National Forest Products Assn. (1984 estimated).

BOARD

Waferboard competes in its uses with the exterior grades of softwood plywood sheathing which represent approximately 80 percent of all softwood plywood production in North America.

	1980	1981	1982	1983	1984
			(billions of square feet)		
Softwood plywood (⅜-inch basis)					
U.S. production	16.7	17.1	17.0	21.0	22.4
Canadian production	2.6	2.4	1.9	2.3	2.1
Waferboard (⅜-inch basis)					
Canadian production	.6	.8	.6	1.0	1.4
U.S. production	.2	.3	.6	1.4	1.7

Sources: Dept. of Industry, Trade and Commerce, American Plywood Assn., FORSIM of Data Resources Inc. (1984 estimated).

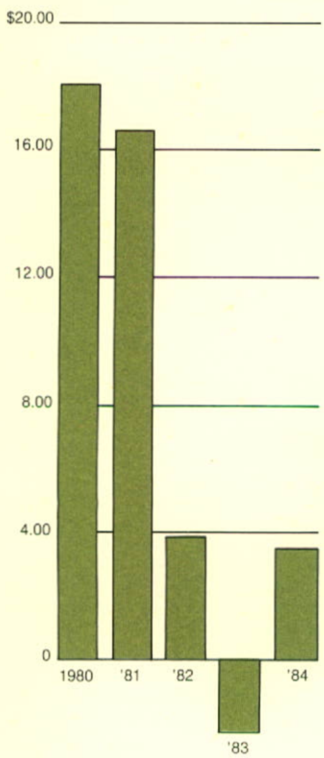
FINANCIAL SUMMARY: LAST FIVE YEARS

Except for per share amounts as indicated, all dollar figures are in thousands	1980	1981	1982	1983	1984
SALES & EARNINGS					
Net sales: pulp and paper	503,861	529,671	416,246	453,185	554,609
building products	35,418	38,923	21,608	41,796	47,367
total	539,279	568,594	437,854	494,981	601,976
Operating profit	174,210	159,930	57,203	35,429	96,144
Interest expense	8,893	8,154	6,630	17,679	24,789
Depreciation	28,375	30,603	33,701	39,863	43,852
Earnings (loss) before income taxes	143,105	130,421	17,350	(22,901)	26,870
Income taxes	61,753	49,400	(1,202)	(12,965)	9,091
Net earnings (loss)	81,352	81,021	18,552	(9,936)	17,779
Net earnings (loss) per share	18.01	16.59	3.80	(2.03)	3.64
Dividends declared, total	9,280	14,164	15,630	5,862	6,350
Dividends per share	2.00	2.90	3.20	1.20	1.30
ASSETS & LIABILITIES					
Current assets	222,455	143,295	151,762	141,796	177,891
Current liabilities	96,726	65,310	102,771	115,101	103,032
Ratio of above assets to liabilities	2.3	2.2	1.5	1.2	1.7
Working capital	125,729	77,985	48,991	26,695	74,859
Inventories, described in balance sheet	64,030	72,940	75,564	72,990	93,553
Fixed assets, see notes to financial statements	508,555	682,667	844,613	892,490	937,689
Accumulated depreciation	210,555	239,946	272,183	309,232	351,443
Long-term debt	70,948	75,597	154,021	171,862	206,841
Ratio of above debt to shareholders' equity	.27	.23	.46	.54	.63
Deferred income taxes	89,613	115,084	134,453	120,942	129,778
Retained earnings at year end	208,519	275,376	278,298	262,500	273,929
EQUITY & OTHER DATA					
Common shares outstanding at year end	4,884,355	4,884,355	4,884,355	4,884,355	4,884,355
Number of shareholders	2,726	2,518	2,397	2,080	1,825
Percentage of shares held in Canada	98.4	98.4	98.4	98.5	98.0
Shareholders' equity, total	263,168	330,025	332,947	317,149	328,578
Shareholders' equity per share	53.88	67.57	68.17	64.93	67.27
Cash flow from operations	119,842	137,095	71,622	16,416	71,448
Cash flow per share	26.53	28.07	14.66	3.36	14.63
Net earnings (loss) percentage on net sales	15.1	14.2	4.2	(2.0)	3.0
Annual expenditures on fixed assets	65,612	189,023	168,765	56,023	47,223
Number of employees on payroll	5,709	5,745	5,246	5,598	5,630

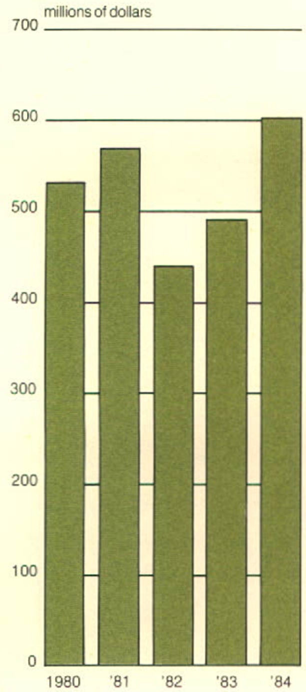
Net earnings per share and cash flow per share are based on the average number of shares outstanding during the year. Dividends per share are based on the number of shares outstanding at the record dates of the dividends. Certain figures for 1980 and 1981 on pages 20 and 21 have been restated from those originally reported to reflect retroactive application of the 1982 change in accounting for investment tax credits.

12

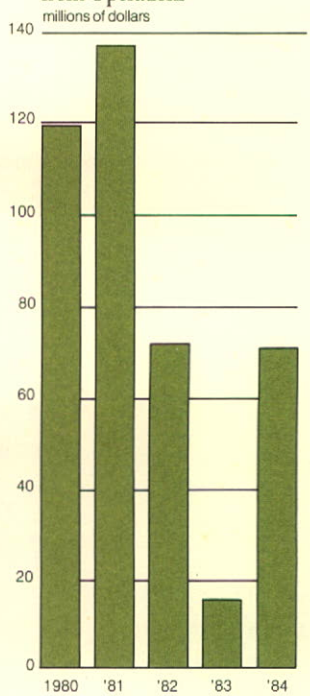
Net Earnings Per Share



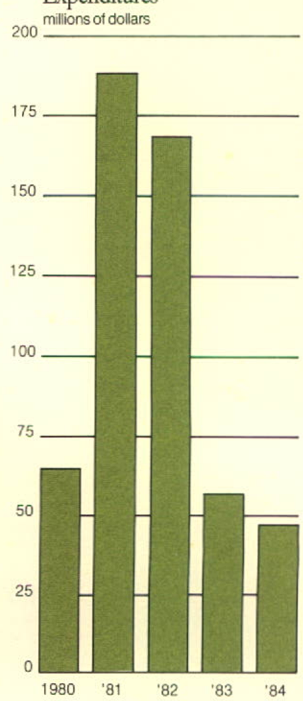
Net sales



Cash Flow from Operations



Capital Expenditures



Results by Quarters

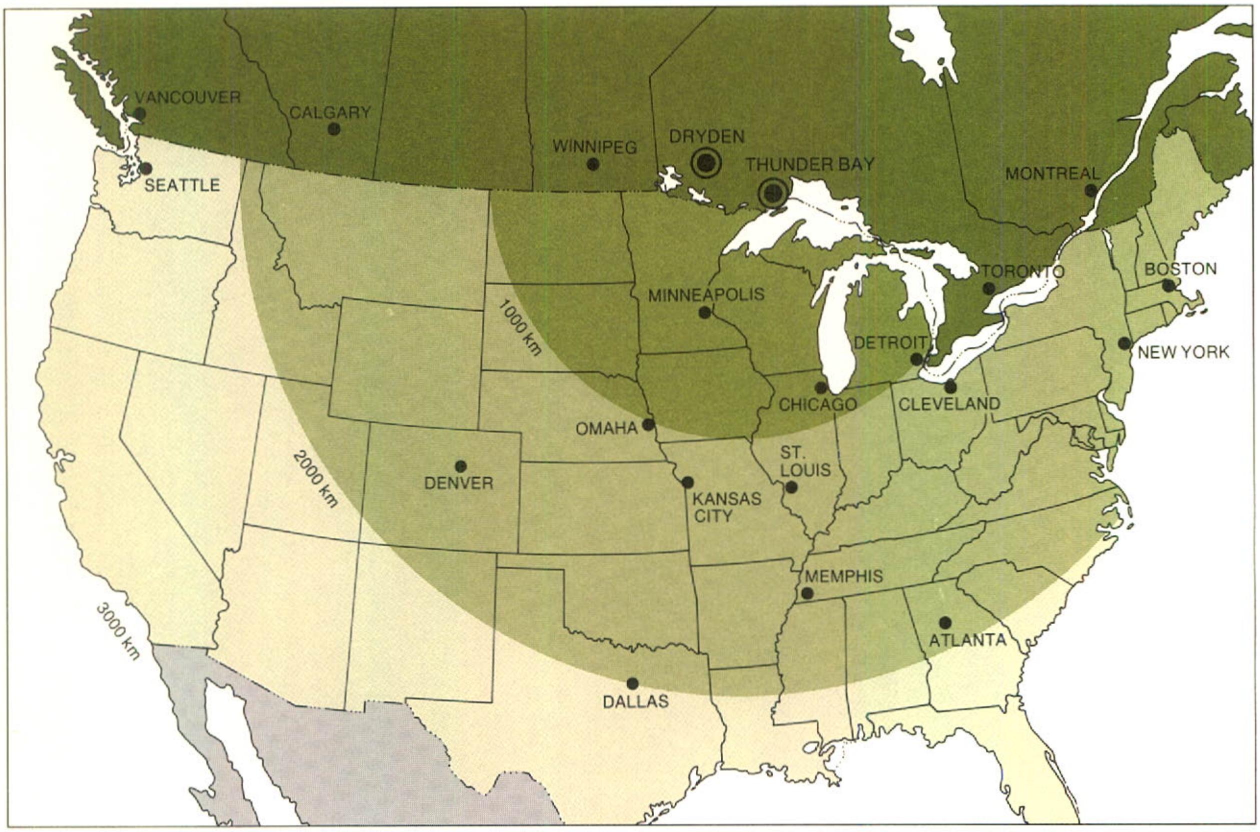
1984 Sales and Earnings
('000 omitted)

Quarter	Net Sales	Oper. Profit	Net Earnings (Loss)
First	$137,068	$13,579	$ 206
Second	157,052	26,103	4,410
Third	152,091	27,816	5,445
Fourth	155,765	28,646	7,718
	$601,976	$96,144	$17,779

Net Earnings (Loss) Per Share

Quarter	1980	1981	1982	1983	1984
First	$ 5.09	$ 4.23	$ 2.95	$(1.58)	$0.04
Second	4.42	4.44	1.56	(0.02)	0.91
Third	4.41	4.07	0.19	(0.07)	1.11
Fourth	4.09	3.85	(0.90)	(0.36)	1.58
	$18.01	$16.59	$ 3.80	$(2.03)	$3.64

OUR MARKETS



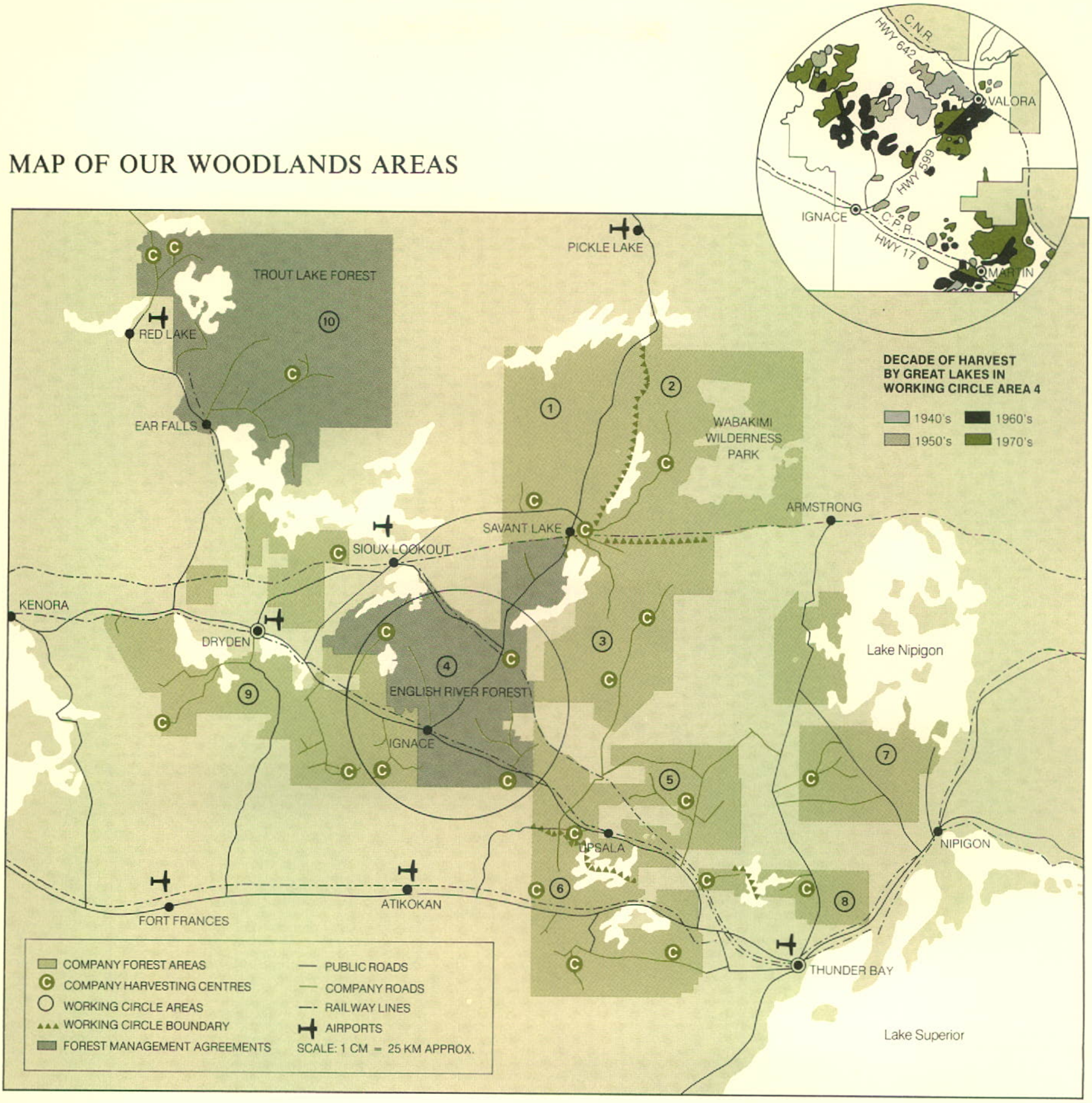
The Thunder Bay and Dryden mills are well situated to serve North American markets. The bulk of our production reaches customers within a radius of 2,000 kilometres of our mills. Virtually our entire newsprint market at present lies within this area. Our kraft pulp production reaches across the whole of the United States and to offshore markets including the Far East. Some of our fine paper production is shipped to the Mid-western 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

	1980	1981	1982	1983	1984
Newsprint (thousands of metric tons)	391	386	360	393	398
Kraft pulp (thousands of metric tons)	521	504	380	531	559
Fine papers (thousands of metric tons)	62	64	44	46	59
Total (thousands of metric tons)	974	954	784	970	1,016
Stud lumber (millions of board feet)	132	137	114	137	162
Waferboard (millions of sq. ft.—⅜-inch basis)	87	86	15	73	107

While waferboard is manufactured in varying thicknesses, for comparative purposes with the industry statistics on page 19, our shipment volume is shown here on a ⅜-inch equivalent basis.

MAP OF OUR WOODLANDS AREAS



The map shows our woodlands areas for both Thunder Bay and Dryden operations. These forest areas encompass some 20,500 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 4,200 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 and Trout Lake Forest shown on the map are under forest management agreements with the Province as discussed on page 5. 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.

Board of Directors at December 31, 1984

C. R. BOWLES *executive vice-president, Great Lakes Forest Products Limited*	Thunder Bay	1964
*R. W. CAMPBELL *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 executive 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
†J. ROSS LEMESURIER *retired investment dealer*	Toronto	1984
†*RICHARD C. MEECH, Q.C. *partner, Borden & Elliot, barristers and solicitors*	Toronto	1980
*B. H. RIDDER, JR. *director, Knight-Ridder Newspapers, Inc.*	St. Paul, Minnesota	1957
BARTLETT B. ROMBOUGH *president and chief executive officer, PanCanadian Petroleum Limited*	Calgary	1984
STANLEY H. STAUFFER *president, Stauffer Communications Inc.*	Topeka, Kansas	1984
WILLIAM W. STINSON *president, Canadian Pacific Limited*	Montreal	1982
J. G. TREZEVANT *consultant, News America Syndicate*	Irvine, California	1975

* *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, 1984

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