

Information Circular and Annual Statutory Report

1989

INFORMATION CIRCULAR AND ANNUAL STATUTORY REPORT FOR 1989 OF MacMILLAN BLOEDEL LIMITED

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AVAILABLE DOCUMENTS

The Company's Annual Report to the United States Securities and Exchange Commission (Form 10-K), Annual Information Form and a copy of this document in French are available to shareholders on request from the Corporate Secretary of the Company at the Company's head office at 1075 West Georgia Street, Vancouver, British Columbia, Canada, V6E 3R9, (604) 661-8302.

This document contains the majority of the information required by the United States Securities and Exchange Commission (Form 10-K). Form 10-K information not included herein is:

1. Cover page.
2. Cross reference index page to Form 10-K Items.
3. Signature page.
4. Item 14 — Exhibits, financial statement schedules and reports on Form 8-K.

**NOTICE OF ANNUAL GENERAL MEETING
OF COMMON SHAREHOLDERS**

To the Common Shareholders of
MacMillan Bloedel Limited:

NOTICE IS HEREBY GIVEN that the Annual General Meeting of the common shareholders of MacMillan Bloedel Limited will be held in the B.C. Ballroom of the Hotel Vancouver, 900 West Georgia Street, Vancouver, B.C. on Thursday, March 29, 1990 at 10:00 a.m. local time, for the following purposes:

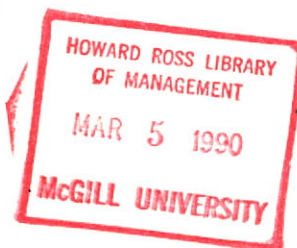
1. To receive and consider the report of the directors and the financial statements of the Company for the year ended December 31, 1989;
2. To elect directors for the ensuing year;
3. To appoint auditors for the ensuing year and to authorize the directors to fix their remuneration; and
4. To transact any other business that may properly be brought before the meeting.

Shareholders who are unable to attend the Annual General Meeting in person are invited to complete the enclosed form of proxy and mail it as soon as possible in the envelope provided.

DATED at Vancouver, B.C. the 21st day of February, 1990.

BY ORDER OF THE BOARD

G.E. MYNETT, FCIS
Corporate Secretary



INFORMATION CIRCULAR
In connection with the meeting to be held on March 29, 1990
Dated as of February 21, 1990

This information circular is furnished in connection with the solicitation by the board of directors of MacMillan Bloedel Limited (the "Company") of proxies for use at the Annual General Meeting of common shareholders to be held on Thursday, March 29, 1990 at the time and place and for the purposes set forth in the notice of the meeting accompanying this information circular.

The persons named in the enclosed form of proxy were designated by the directors of the Company. **A shareholder desiring to appoint some other person to represent him at the meeting may do so either by writing such person's name on the form of proxy or by completing another proper form of proxy. A person appointed as a proxy need not be a shareholder of the Company.** All completed proxy forms must be deposited with Central Guaranty Trust Company, 800 West Pender Street, Vancouver, B.C. or the Corporate Secretary of the Company, not less than 48 hours before the time of the meeting. The form of proxy must be signed by the shareholder or by his attorney authorized in writing, or, if the shareholder is a corporation, by an officer or by the duly authorized attorney of the corporation. A shareholder who has given a proxy may revoke it at any time before it is exercised. Attendance at the meeting and participation in a poll by a shareholder automatically revokes the proxy. If a poll is taken and if the instructions are certain, the persons named in the enclosed form of proxy will vote the shares in respect of which they are appointed in accordance with the direction of the shareholders appointing them. **In the absence of such direction such shares will be voted on a poll in favour of each of the nominees for election as directors and for each other matter shown on the form of proxy.** The form of proxy enclosed, when properly signed, confers discretionary authority with respect to amendments or variations of the matters identified in the notice of meeting and any other matters that may properly be brought before the meeting. At the time of printing this information circular, the directors of the Company are not aware that any such variations or other matters are to be presented for action at the meeting.

The resolutions to be presented to the meeting are ordinary resolutions which require the affirmative votes of the holders of a majority of the shares represented in person or by proxy.

This solicitation is being made by mail and the cost will be borne by the Company. Shareholder Communications Corporation was retained to assist the Company in the solicitation of proxies in the United States at a fee of approximately U.S. \$4,000.

RECORD DATE AND ADVANCE NOTICE

The record date for determining the names of common shareholders entitled to the notice of meeting and this information circular was fixed as the close of business on February 8, 1990. At the date of the Annual General Meeting, each person who is then entered in the register of members of the Company as a holder of one or more common shares shall be entitled to attend the meeting in person or by proxy and in the event of a poll to cast one vote for each share.

VOTING SHARES AND PRINCIPAL HOLDERS THEREOF

The Company has outstanding as of February 1, 1990 and entitled to be voted at the meeting 102,649,825 common shares, each share carrying the right to one vote. This figure includes 552 shares represented by warrants.

To the knowledge of the directors and officers of the Company at the date hereof, no person or company owns, directly or indirectly, or exercises control over, shares carrying more than 5% of the voting rights attaching to all common shares of the Company entitled to be voted at the meeting except as set out below.

Title of class	Name and address of beneficial holder	Amount beneficially owned	Percentage of class
		Feb. 1, 1990	
Common shares	Noranda Forest Inc., Suite 4414, Toronto Dominion Bank Tower, Toronto Dominion Bank Centre, Toronto, Ontario, M5K 1A1	51,193,663	49.9%

685,142 common shares (less than 1% of class) were owned beneficially by the directors and executive officers as a group (including qualifying shares).

DIRECTORS' MEETINGS

The board of directors of the Company consists of sixteen members, presently made up of four executive officers and twelve directors who are not executive officers. The board of directors held six meetings during 1989. The board appoints from among its members committees with responsibility to perform specific functions. These committees include an executive committee, an audit committee, a compensation committee and a nominating committee. The executive committee, during the intervals between the meetings of the board, possesses and may exercise, subject to any restrictions imposed by the board, the articles or by law, all the powers of the board in the management of the business of the Company. Six meetings of the executive committee were held during 1989.

The audit committee assists the board in fulfilling its responsibilities relating to financial accounting and reporting practices; reviews any financial statement to be included in any prospectus or to be presented at an annual general meeting; considers the report of the external auditors on its financial statements; reviews the overall integrated audit plan of its internal and external auditors and receives their reports on the assessment of financial accounting controls and the adequacy of the Company's record keeping; examines the fees and expenses for both audit and non-audit services; recommends to the board a firm of independent auditors for appointment by the shareholders; and receives and reviews at least annually the chief executive officer's certificate under the Company's code of corporate behavior. Three meetings of the audit committee were held during 1989.

The compensation committee determines, within the framework of the basic compensation policy established by the board, the salary scales and general salary structures, fixes the salaries of the chairman, vice-chairman, president and executive vice-president and on the recommendation of the chief executive officer approves the salaries of all officers of the Company. It also oversees the administration of the Company's benefit programs for salaried employees, the employee share purchase plan, pension plan, management incentive compensation plan and senior management share purchase plan. Two meetings of the compensation committee were held during 1989.

The nominating committee recommends to the board the size and composition of the board and the names of persons to be nominated as directors for the ensuing year or to fill casual vacancies as they occur during the year. One meeting was held during 1989. The advance notice of the Annual General Meeting to be held on Thursday, March 29, 1990, which was published in Vancouver on February 1, 1990, included an invitation for written nominations signed by members holding in the aggregate not less than ten percent of the Company's common shares for inclusion in this information circular. No such nominations had been received by February 21, 1990.

In addition to the above committees of the board there is also an environmental committee, a donations committee and a pension fund investment advisory committee.

Each of the directors except Messrs. Eyton, Harrison, Powis and Walton attended 75% or more of the total number of meetings of the board and the committees on which he or she serves. Directors who were unable to attend or participate in meetings held by conference telephone were informed of the matters to be discussed, had an opportunity to express their views and to review the minutes of the meetings and, in most instances in respect of committees, were represented by alternate directors.

ELECTION OF DIRECTORS

The persons named in the enclosed form of proxy intend, unless otherwise directed, to vote for the election of a board of directors composed of the sixteen nominees in the list below. If any nominee does not stand for election or is unable to serve, proxies may be voted for a smaller board at the discretion of the person exercising the proxy vote. Each director elected will hold office until the conclusion of the next Annual General Meeting, unless his office is earlier vacated in accordance with applicable law or the Articles of the Company.

INFORMATION CONCERNING NOMINEES

<u>Name and residence</u>	<u>Principal occupation of nominee during the past five years</u>	<u>Age at Feb. 1, 1990</u>	<u>Director since</u>	<u>Shares held*</u>
D.C. Davenport Vancouver, Canada	Partner of Davis & Company (barristers and solicitors). (Notes 1, 2, 4 and 7)	57	1981	525
F.J. de Wit Blaricum, The Netherlands	Chairman, Board of Management, Koninklijke Nederlandse Papierfabrieken N.V. (manufacturers of fine and coated papers). (Note 4)	50	1986	3,381
J.T. Eyton, O.C. Caledon, Canada	President and Chief Executive Officer, Brascan Limited (natural resources, financial services and consumer products). (Notes 4 and 5)	55	1985	9,120
R.E. Harrison Toronto, Canada	Corporate Director since 1985; prior to which he was Chairman, Canadian Imperial Bank of Commerce. (Notes 1, 4 and 5)	68	1981	5,019
G.H.D. Hobbs Vancouver, Canada	Corporate Director. (Notes 1, 3 and 4)	68	1972	7,200
R.T. Kenny Buckingham, Canada	President and Chief Operating Officer, Noranda Forest Inc. (forest products) and Senior Vice-President — Forest, Noranda Inc. (mining and metallurgy, manufacturing, forest products, oil and gas exploration) since 1986; prior to which he was President and Chief Executive Officer, James MacLaren Industries Inc. (forest products). (Notes 4 and 7)	60	1986	1,826
D.W. Kerr Toronto, Canada	President, Noranda Inc. (mining and metallurgy, manufacturing, forest products, oil and gas exploration) since 1987; prior to which he was Senior Vice-President, Strategic Planning, Noranda Inc. from 1986; prior to which he was Executive Vice-President, Brascan Limited from 1985; prior to which he was Chief Operating Officer, Hees International Corporation. (Notes 2 and 4)	46	1988	5,000
C.C. Knudsen Seattle, U.S.A.	Vice-Chairman of the Board. (Notes 1, 2 and 4)	66	1976	14,259
D.L. McLauchlin Vancouver, Canada	Executive Vice-President since 1989; prior to which he was Executive Vice-President, Operations of the Company. (Note 7)	63	1988	48,989
J.A. Pattison West Vancouver, Canada	Chairman, President and Chief Executive Officer, The Jim Pattison Group Inc. (holding company). (Notes 3, 4 and 5)	61	1987	3,596

<u>Name and residence</u>	<u>Principal occupation of nominee during the past five years</u>	<u>Age at Feb. 1, 1990</u>	<u>Director since</u>	<u>Shares held*</u>
A. Powis, O.C. Toronto, Canada	Chairman and Chief Executive Officer, Noranda Inc. (mining and metallurgy, manufacturing, forest products, oil and gas exploration). (Notes 3 and 4)	59	1981	5,315
R.V. Smith West Vancouver, Canada	President and Chief Executive Officer of the Company. (Notes 1, 4 and 5)	63	1980	102,478
Jean M. Southam Vancouver, Canada	Private Investor; Trustee, Lester B. Pearson College of the Pacific; Governor, Vancouver Public Aquarium; Member of the Board, World Wildlife (Canada). (Notes 4 and 6)	74	1981	61,640
Dr. D.W. Strangway Vancouver, Canada	President of The University of British Columbia since 1985; prior to which he held various positions with the University of Toronto including that of President. (Notes 2, 4, 6 and 7)	55	1986	801
J.S. Walton Vancouver, Canada	President, Endeavour Capital Corporation, since July 1989, (corporate & financial advisory services); Corporate Director since 1988; prior to which he was President and Chief Executive Officer, Placer Dome Inc. (international mining) since 1987; prior to which he was President and Chief Executive Officer, Placer Development Limited (mining, oil and gas) from 1985; prior to which he was Executive Vice-President, Corporate and a Director of Westmin Resources Inc. (natural resources). (Notes 3, 4 and 7)	59	1988	2,000
A.H. Zimmerman Toronto, Canada	Chairman of the Board of the Company; Chairman and Chief Executive Officer, Noranda Forest Inc. (forest products). (Notes 1, 3 and 4)	62	1981	30,096

*This column shows the number of common shares (including 500 qualifying shares), as reported to the Company, beneficially owned directly or indirectly or over which control is exercised by each of the nominees. The percentage of shares other than qualifying shares held by each nominee is in no case greater than .1 percent.

- Note: (1) Member of the Executive Committee
(2) Member of the Audit Committee
(3) Member of the Compensation Committee
(4) Member of the Nominating Committee
(5) Member of the Pension Fund Investment Advisory Committee
(6) Member of the Donations Committee
(7) Member of the Environmental Committee

The directors listed below hold directorships in other companies with a class of securities registered pursuant to Section 12 of the United States Securities Exchange Act of 1934 or which are subject to the requirements of Section 15(d) of such Act or which are registered as investment companies under the United States Investment Company Act of 1940:

J.T. Eyton, O.C.	M.A. Hanna Co. (plastics and mining) Norcen Energy Resources Limited (oil and gas) Scott Paper Company (tissue products and fine papers)
R.E. Harrison	Campbell Soup Co. Ltd. (food products) Trans Canada Pipelines Limited (oil and gas transmission, exploration and production)
G.H.D. Hobbs	British Columbia Telephone Company (utilities)
D.W. Kerr	Norcen Energy Resources Limited (oil and gas) North Canadian Oils Ltd. (oil and gas)
C.C. Knudsen	Cascade Corporation (components for heavy industrial equipment) Penwest Ltd. (brewers' malt and corn derivatives) Portland General Corporation (utilities holding) Portland General Electric (utilities) Safeco Corporation (insurance) Security Pacific Bancorporation Northwest (bank holding) Security Pacific Bank Washington N.A. (banking) Security Pacific Corporation (bank holding) Security Pacific National Bank (banking)
J.A. Pattison	Paramount Communications (entertainment, publishing, financial services) Henley Group Inc. (diversified manufacturing)
A. Powis, O.C.	Gulf Canada Corporation (oil and gas, forest products, distilled spirits) G.W. Utilities Limited (diversified holding company) M.A. Hanna Co. (plastics and mining) Norcen Energy Resources Limited (oil and gas) North Canadian Oils Limited (oil and gas)
A.H. Zimmerman.....	The Pittston Company (coal mining, air freight, armoured transport and security services)

BUSINESS RELATIONSHIPS

In the ordinary course of business, the Company has transactions with various companies and firms of which certain of its directors are officers or directors. None of these transactions, however, has been material to the Company and the Company believes that they have not been material to the other companies or firms involved. During the year and in the ordinary course of business, the Company consulted and is continuing to consult Davis & Company, a law firm of which D.C. Davenport is a partner.

APPOINTMENT OF AUDITORS

The persons named in the enclosed form of proxy will, unless otherwise directed, vote for the re-appointment of Price Waterhouse as auditors of the Company for the ensuing year, with authority to the directors to set their fees. Representatives of this firm will be present at the Annual General Meeting to respond to questions asked at the meeting and will have the opportunity to make a statement if they see fit.

1991 ANNUAL GENERAL MEETING

Proposals of shareholders intended to be presented at the Annual General Meeting to be held in 1991 must be received by the Company for inclusion in the information circular for that meeting by October 25, 1990.

EXECUTIVE COMPENSATION

(a) Current cash compensation

The following table shows cash compensation paid and accrued for services in 1989 for each of the five most highly compensated executive officers of the Company and for all executive officers of the Company as a group:

Cash Compensation Table

Name of individual or number in group	Capacities in which served	Cash salaries	Cash bonuses
R.V. Smith	President and Chief Executive Officer	\$ 330,000	\$ 295,000
D.L. McLauchlin	Executive Vice-President	\$ 240,000	\$ 172,800
J. St. C. Ross	Senior Vice-President, Regional Operations	\$ 280,234	\$ 176,200
R.B. Findlay	Senior Vice-President, Marketing	\$ 275,870	\$ 171,600
R.N. Wiewel	Senior Vice-President, Product Development	\$ 182,974	\$ 158,100
27	All executive officers as a group (including the five individuals named above)	\$3,884,608	\$2,712,522

This table includes persons who ceased to be executive officers during the year, but excludes 1989 benefits of \$124,428 not available to all employees. The amounts included relate only to the portions of the year during which the executive officers were actually in office.

(b) Compensation pursuant to plans

Remuneration payments made in 1989 pursuant to the plans described below and proposed to be made in the future to the executive officers listed in section (a) are as follows:

(1) Management Incentive Compensation Plan

The Company has a management incentive compensation plan which applies to a number of key employees throughout the Company. The plan provides for the creation of an annual fund equal to 4% of adjusted consolidated net earnings in excess of a percentage (9% in 1989) of the average consolidated capital employed, or as determined by the compensation committee of the board of directors. It also provides for distribution of all or part of that fund to participants according to individual and unit performance without carryover to future years. 1989 amounts accrued for executive officers are included as Cash bonuses in the Cash Compensation Table.

(2) Senior Management Share Purchase Plan

The Company has a senior management share purchase plan which is intended to provide a long term incentive and capital appreciation opportunity for selected key employees of the Company directly related to corporate performance and to the market price of the Company's shares. Between March 1 and June 30 of each year, participants may have the opportunity to buy a specified number of shares at the then current market price on The Toronto Stock Exchange. The number of shares which each participant may buy under the plan depends on the Company's return on investment for the previous year, the participant's salary during such year and the share price. The purchase is financed by a ten year non-recourse interest-free loan granted to the participant by the Company and secured by a pledge of the shares. Cash dividends on the pledged shares are applied to reduce the loan. At any time within the ten year period the participant may repay the loan and take possession of the pledged shares. Shares issued during 1989 to the five named individuals were R.V. Smith 27,905 shares (\$523,498), D.L. McLauchlin 14,840 shares (\$278,398), J.St.C. Ross 10,875 shares (\$204,015), R.B. Findlay 10,215 shares (\$191,633), R.N. Wiewel 10,875 shares (\$204,015) and other executive officers 107,010 shares (\$2,007,507). There were no shares received or loans repaid during the year. Common shares held and loans outstanding as at December 31, 1989 by the five named individuals were R.V. Smith 70,327 shares (\$1,185,687), D.L. McLauchlin 46,176 shares (\$762,446), J.St.C. Ross 36,065 shares (\$579,802), R.B. Findlay 27,040 shares (\$484,895), R.N. Wiewel 35,411 shares (\$574,449) and other executive officers 262,005 shares (\$4,598,445). The market price for the Company's common shares on February 1, 1990 was \$17.00 per share.

(3) *Noranda Share Purchase Plan*

Noranda Inc. has a share purchase plan which is offered by the directors of Noranda Inc. to senior employees of subsidiary or affiliated companies, and is intended to provide an opportunity for capital appreciation to key employees. Participants have the opportunity to purchase shares of Noranda Inc., financed by a seven year interest-free recourse loan provided by Noranda Inc., and secured by a promissory note and the shares which are held as collateral. The participant is entitled to receive dividends on the shares, but is not required to apply cash dividends to reduce the outstanding loan. The participant may repay the loan at any time within the seven year period and take possession of the pledged shares. No shares were issued under the plan during 1989. Shares received during 1989 by the named individuals were J.St.C. Ross 2,690 shares (\$50,973 loan repaid), R.N. Wiewel 2,690 shares (\$50,973 loan repaid) and other executive officers received 8,420 shares (\$157,385 loans repaid). Common shares held and loans outstanding as at December 31, 1989 by other executive officers were 2,234 shares (\$45,243). The market price for Noranda Inc.'s common shares on February 1, 1990 was \$21.25 per share.

(4) *Stock Option and Stock Appreciation Rights Plans*

The Company has a stock option plan for selected employees under which options on common shares or stock appreciation rights may be granted to selected key employees. The plan is administered by a committee appointed by the board of directors. The number of participants in the plan is limited to 150 and the aggregate number of shares in respect of which options or stock appreciation rights may be outstanding is 200,000 shares. Each option granted shall be for a period not exceeding five years. The committee may grant to optionees stock appreciation rights which may be surrendered for cash, and may accept shares owned by an optionee at market price in exchange for options or stock appreciation rights under the plan. No stock options or stock appreciation rights were granted during 1989. No options are outstanding.

(5) *Retirement Plans*

The estimated annual pension benefits payable upon normal retirement to the twenty-seven executive officers covered by the Cash Compensation Table are \$3,644,222 based upon remuneration received and accrued to December 31, 1989.

- (i) As at December 31, 1989, twenty-four executive officers were members of the executive pension plan under which executive officers retire at age 65 with a monthly pension amounting to 2% for each accredited year of service to a maximum of thirty-five years applied to the average monthly salary and bonus during the thirty-six consecutive months when the salary and bonus was highest, with a widow's benefit of 50% of the employee's pension.

The following table sets forth various annual retirement benefits that become payable under the Company's executive pension plan. Benefits are not reduced by government pension payments.

Annual Average covered remuneration	Years of service					
	10	15	20	25	30	35
\$100,000	\$ 20,000	\$ 30,000	\$ 40,000	\$ 50,000	\$ 60,000	\$ 70,000
\$150,000	\$ 30,000	\$ 45,000	\$ 60,000	\$ 75,000	\$ 90,000	\$105,000
\$200,000	\$ 40,000	\$ 60,000	\$ 80,000	\$100,000	\$120,000	\$140,000
\$250,000	\$ 50,000	\$ 75,000	\$100,000	\$125,000	\$150,000	\$175,000
\$300,000	\$ 60,000	\$ 90,000	\$120,000	\$150,000	\$180,000	\$210,000
\$350,000	\$ 70,000	\$105,000	\$140,000	\$175,000	\$210,000	\$245,000
\$400,000	\$ 80,000	\$120,000	\$160,000	\$200,000	\$240,000	\$280,000
\$450,000	\$ 90,000	\$135,000	\$180,000	\$225,000	\$270,000	\$315,000
\$500,000	\$100,000	\$150,000	\$200,000	\$250,000	\$300,000	\$350,000
\$550,000	\$110,000	\$165,000	\$220,000	\$275,000	\$330,000	\$385,000
\$600,000	\$120,000	\$180,000	\$240,000	\$300,000	\$360,000	\$420,000
\$650,000	\$130,000	\$195,000	\$260,000	\$325,000	\$390,000	\$455,000

As at December 31, 1989, R.V. Smith had 31 years of service with the Company, D.L. McLaughlin had 37 years of service with the Company, J.St.C. Ross had 25 years of service with the Company, R.N. Wiewel had 22 years of service with the Company and R.B. Findlay had 24 years of service with the Company.

- (ii) As at December 31, 1989, one executive officer had a service agreement with the Company pursuant to which he agrees to retire at age 65, and the Company agrees to pay him a monthly pension at the rate of 50% of his average monthly pensionable earnings and to pay to his widow a pension of 50% of his pension. Pensionable earnings are earnings for the thirty-six consecutive months during which his salary plus 50% of his bonus was highest. This service agreement provides for termination prior to age 65 by either party on six months' notice. Under certain circumstances he will be entitled to the pension calculated as above or as reduced by a formula based on age and years of service under contract. Benefits are not reduced by government pension payments. Two executive officers with service agreements retired during 1989.

(c) Remuneration of directors

Directors who are not in receipt of salaries as executive officers of the Company or its subsidiaries are each paid an annual retainer of \$8,000 and \$1,500 for each board meeting attended. Members of the executive committee who are not in receipt of salaries are each paid \$1,000 for each meeting attended. Directors who are not in receipt of salaries acting on other committees of the board are paid \$750 for each meeting attended, except for the nominating committee in respect of which no fees are paid. Committee chairmen receive an additional fee of \$125 for each meeting attended, except for the chairman of the audit committee who receives an additional fee of \$750. In addition the directors are reimbursed for their reasonable expenses in connection with such meetings. The annual retainer portion of the directors' fees is paid, at the directors' option in cash or half in cash and half in common shares of the Company. During 1989, \$233,975 was paid and 1,258 shares were allocated to directors.

1989 ANNUAL STATUTORY REPORT

GLOSSARY OF TERMS

MEASUREMENTS

fbm	— foot-board measure (board foot) — one square foot of lumber one inch thick
hectare	— 2.471 acres
m ³	— cubic metre or 35.315 cubic feet
M cubic feet	— thousand cubic feet
Mfbm (MMfbm)	— thousand (million) feet board measure
MM sq.ft. ¾"	— million square feet, ¾ inch thick used to measure panelboard volumes
tonne	— metric ton — 1,000 kilograms or 2,204 pounds
annual capacity at year end	— the number of units which can be produced in a year based on operations over a long term period and the normal number of shifts and maintenance interruptions
capacity utilization	— production divided by the annual capacity averaged over the production period

PRODUCTS

Pulp

Bleached pulp	— pulp that has been brightened using bleaching chemicals
Chemi-thermomechanical pulp	— pulp produced from wood chips using heated mechanical and chemical processes to break the bonds between the wood fibres
Chemical pulp	— pulp produced from wood chips using chemical processes to break the bonds between the wood fibres
Groundwood pulp	— pulp produced by grinding blocks of wood to break bonds between wood fibres
Kraft or sulphate pulp	— chemical pulp produced by an alkaline cooking process using sodium sulphate
Market pulp	— pulp sold on the open market between non-affiliated companies
Mechanical pulp	— pulp produced from roundwood or woodchips by mechanically breaking the bonds between wood fibres
Softwood pulp	— pulp produced from coniferous wood species noted for its strength

Paper

Coated paper	— paper which is coated with clay and treated to impart a smooth glossy surface
Groundwood and specialty printing paper	— paper with mechanical pulp as its major component which differs from newsprint in brightness, surface characteristics and end uses
Newsprint	— paper produced principally from mechanical pulp for use in newspapers
Fine paper	— paper with bleached chemical pulp as its major component

Building Materials

Dimension lumber	— lumber cut and planed to standard sizes and lengths nominally 2 × 4 inches through 2 × 12 inches in cross section by 8 to 24 feet in length
Panelboard	— comparatively thin flat sheets of wood used for paneling
Particleboard	— panelboard produced by chemically bonding small wood shavings and sawdust under pressure
Plywood	— laminated veneers of solid wood
Waferboard	— panelboard produced by chemically bonding wafers of wood under pressure
Parallam®	— reconstituted lumber manufactured by bonding long strands of veneer into structural beams using waterproof adhesives
Structural panelboard	— plywood, waferboard and particleboard

Containerboard and Packaging

Containerboard	— linerboard and corrugated medium used to produce corrugated boxes (containers)
Corrugated containers	— paper boxes using sheets of linerboard with medium corrugated (fluted) between the linerboard

CORPORATE PROFILE

MacMillan Bloedel Limited (the "Company"), a British Columbia corporation, is a corporation resulting from the amalgamation of MacMillan Bloedel Limited, incorporated under the laws of the Province of British Columbia by Memorandum of Association registered July 13, 1911, and certain of its wholly-owned subsidiaries.

The Company together with its subsidiaries ("MacMillan Bloedel" or "MB") is one of North America's largest forest products companies, with integrated operations in Canada and the United States as well as major investments in Canada, the United Kingdom and Continental Europe. MB manages 1.6 million hectares of productive timberlands which supply most of its fibre requirements. Of these timberlands, one million hectares are in British Columbia where approximately two-thirds of MB's property, plant and equipment and the Company's head office are located. The products of MacMillan Bloedel and its affiliated companies which are marketed throughout the world include lumber, panelboards, kraft pulp, newsprint, groundwood printing papers, fine papers, containerboard and corrugated containers.

The following table summarizes total revenue, contributions to earnings and assets for each of MB's three industrial segments during the last three years:

	Building materials	Pulp and paper	Containerboard and packaging (\$ millions)	Other	Total operations
Total revenue —					
1989	1,408.6	1,310.2	504.1	50.8	3,273.7
1988	1,404.7	1,282.5	530.1	56.2	3,273.5
1987	1,429.8	1,145.3	506.1	53.3	3,134.5
Contributions to earnings —					
1989	139.1	180.8	113.6	2.3	435.8
1988	186.8	254.9	118.0	3.9	563.6
1987	206.4	229.6	88.9	4.5	529.4
Assets —					
December 31, 1989	1,161.3	1,081.1	473.1	28.0	2,743.5
December 31, 1988	960.9	922.7	443.8	32.1	2,359.5
December 31, 1987	827.7	779.6	429.4	32.4	2,069.1

MB also owns substantial interests in companies operating in related fields, which are described under Investments on page 21 of this report.

Further financial information and explanatory notes pertaining to each of MB's industry and geographic segments and export sales are presented in Note 16 of notes to consolidated financial statements included on pages 52 and 53 of this report.

BUILDING MATERIALS

Logging Operations

MB has a number of operations, primarily on the coast of British Columbia and in Alabama, which harvest logs to supply the wood fibre requirements of its converting plants. In order to extract maximum value, the logs are directed to the converting unit according to species, size and quality. Imbalances in supply and demand are adjusted by sales and purchases of logs in the open market. High quality logs are used mainly in the manufacture of lumber. Lower quality logs, together with small or defective parts of trees and chips from plywood and sawmill operations, form the basic raw material supply for the pulp and paper, and containerboard mills. Wood waste, principally sawdust and bark, is used to produce energy required by the converting facilities.

The following table shows the volumes of logs harvested as part of the activity of supplying the fibre requirements of MB's major converting facilities in each of the years 1989, 1988 and 1987:

	Year ended December 31		
	1989	1988	1987
	(thousands of cubic metres)		
British Columbia	7,849	7,959	8,456
Alabama and Mississippi (includes hardwood)	880	877	940

Reforestation

In order to assure a continuing supply of raw materials for the future, the Company maintains an active reforestation program in British Columbia.

In 1988 the British Columbia Forest Act was amended to transfer financial responsibility for reforestation on Crown lands to licencees for lands logged after October 1, 1987.

The Company operates the A.P. MacBean Nursery which coupled with tree improvement and reforestation research provides healthier, faster-growing seedlings for planting on Company-managed lands. Company managed lands in British Columbia in the process of being restocked currently represents about three years of logging which is reflective of the restocking process and consistent with the Company's experience over the last two decades. This is considered very commendable in all forestry circles.

MB also carries out reforestation in Alabama. An integral part of this is the nursery and seed orchard which provides high-quality, genetically superior seedlings. The Robert E. Mitchell Tree Nursery has an annual crop of over 36 million top quality seedlings which are planted on MB controlled forest lands or sold commercially.

Forest Lands

The total area of commercial forest lands under MB's control is:

	Commercial hectares	
	(Note 1)	
British Columbia: (Note 2)		
Area operated on a sustained yield basis:		
Tree-farm licences: (Note 3)		
Crown lands (Note 4)	653,000	
Timber licences (Note 5)	126,000	
Owned lands (Note 6)	<u>78,000</u>	
	857,000	
Managed forest lands (owned lands) (Note 6)	<u>144,000</u>	1,001,000
Other tenures:		
Timber licences (Note 7)	47,000	
Owned lands	<u>3,000</u>	<u>50,000</u>
		1,051,000
Saskatchewan (Note 8)		324,000
Alabama and Mississippi: (Note 9)		
Owned lands	79,000	
Long term cutting rights	<u>103,000</u>	<u>182,000</u>
		1,557,000

Notes:

- (1) Land is considered commercial if it is feasible to grow timber on it which can be economically harvested using present technology. Lands controlled by MB in Alabama, Mississippi and Saskatchewan are considered commercial. In British Columbia 56,000 hectares controlled by MB are considered inaccessible and hence not commercial.
- (2) The Government of British Columbia owns approximately 95 percent of all forest lands in the province. Under the Forest Act, the Government is empowered to grant "tree-farm licences" to a licensee who undertakes to manage an area of Government owned forest land, often in combination with adjacent forest land held by the licensee, to yield an annual crop on a sustained yield basis (i.e. in perpetuity).

Effective January 1, 1989, MB's available annual allowable cut from accessible timberlands operated on a sustained yield basis has been 7.5 million cubic metres. In 1988, the B.C. Forest Act was amended to remove 5 percent of the Crown annual allowable cut from licence holders which reduced the cut available to MB by 265,000 cubic metres annually. The reduced Crown cut, together with timber harvested from other MB tenures, is sufficient to provide on average about 80 percent of the wood requirements (logs and chips) for the present production facilities in British Columbia. When the Forest Act was amended, the direct financial

responsibility for reforestation of Crown lands logged after October 1, 1987 was shifted from the Government to the industry.

- (3) The tree-farm licences contain a number of areas which are subject to action by various interest groups intent upon having those lands withdrawn from timber production:

	Commercial hectares	Action by
Carmanah Valley	6,616	Special interest groups
Clayoquot Sound*	106,026	Special interest groups and Native Indians*
Other areas	20,680	Special interest groups
	<u>133,322</u>	

*Includes Meares Island with 3,573 commercial hectares subject to a court injunction on behalf of Native Indians.

The Company believes most of these activities against the contractual rights of the Company will be resolved in a manner acceptable to the Company either by full endorsement of the Company's rights, exchange of equal value property and cutting rights or modest and appropriate designation of restricted areas as wilderness preserves. (MB's first and most famous preserve is Cathedral Grove, near Alberni in British Columbia, established in 1945).

- (4) These are contained within MB's two tree-farm licences. These tree-farm licences were renewed for 25 year terms in the early 1980's.
- (5) The Company owns standing timber on the land held under timber licences. A royalty is payable upon harvesting the timber. After the timber is harvested on these lands, the Company has the responsibility to reforest them. They then revert to the Crown but will be retained within the tree-farm licences as "Crown lands". Approximately 29,500 hectares of these lands have been logged but not reverted.
- (6) Certain owned lands have been put into tree-farms, known as "managed forest lands", by the Company to obtain an incentive property tax rate.
- (7) Included are approximately 15,000 hectares of lands which already have been logged and will revert to the Crown when restocked at the Company's expense.
- (8) MB's cutting rights in Saskatchewan, which are limited to species used by the waferboard plant at Hudson Bay, Saskatchewan, are held under a forest management licence expiring in 1994. The licence is renewable for 20 year periods on terms and conditions to be negotiated at the time of renewal. These resources are sufficient to supply the fibre requirements of the waferboard plant.
- (9) The wood supply from its own timber resources (41% in 1989) together with outside purchases are sufficient for the present operations of the Pine Hill, Alabama mills. In 1989 MB purchased 11,193 hectares of timberlands to further support the Pine Hill mills.

Stumpage and Royalty

A stumpage charge that will generate a revenue target for the British Columbia Government is assessed by the Government on all Crown timber harvested.

On those lands held under timber licences a fixed royalty is payable when the timber is harvested.

No royalty or stumpage charges are payable on timber harvested on Company owned lands.

In Saskatchewan, stumpage rates have been confirmed at the present fixed rate level to June 30, 1994.

Building Materials Manufacturing Operations

MB manufactures a wide variety of building materials products including lumber, plywood, waferboard, particleboard and Parallam® and carries on wholesale building materials distribution businesses. MB also purchases significant amounts of lumber from other suppliers for resale, utilizing its marketing and transportation services. For the years ended December 31, 1989, 1988 and 1987 lumber accounted for 30.8%, 30.8% and 32.6% respectively of MB's consolidated sales values to unaffiliated customers. By-products of building materials production include wood chips which are an important raw material for the Company's pulp and paper mills and also sawdust and bark which are a significant source of energy for the mills.

Building Materials Facilities

MB operates the following converting facilities for the manufacture of building materials:

	<u>Division</u>	<u>Location</u>	<u>Annual capacities at year-end 1989</u>	<u>1989 Production</u>
Lumber & Lumber Specialties (MMfbm)	Alberni Pacific	Port Alberni, British Columbia	250	161
	Somass*	Port Alberni, British Columbia	120	92
	Northumberland*	Nanaimo, British Columbia		
	Island Phoenix		155	14
	Thunderbird		149	131
	Chemainus	Chemainus, British Columbia	106	101
	Canadian White Pine	Vancouver, British Columbia	118	128
	New Westminster*	New Westminster, British Columbia	110	76
	Powell River	Powell River, British Columbia	49	33
	Pine Hill	Pine Hill, Alabama	80	56
			<u>1,137</u>	<u>792</u>
Plywood (MM sq.ft. 3/8")	Alberni Plywood	Port Alberni, British Columbia	175	108
	Pine Hill	Pine Hill, Alabama	133	107
	Nipigon	Nipigon, Ontario	30	25
			<u>338</u>	<u>240</u>
Waferboard (MM sq.ft. 3/8")	Hudson Bay	Hudson Bay, Saskatchewan	<u>191</u>	<u>205</u>
Particleboard (MM sq.ft. 3/4")	Particleboard	Vancouver, British Columbia	<u>57</u>	<u>49</u>
Hardboard (MM sq.ft.)	Sturgeon Falls	Sturgeon Falls, Ontario	<u>47</u>	<u>22</u>
Parallam® (M cubic feet)	Parallam®	New Westminster, British Columbia	<u>980</u>	<u>455</u>
Specialty Board (MM sq.ft.)	Specialty Board	Vancouver, British Columbia	<u>37</u>	<u>18</u>
Mouldings (MM lineal ft.)	Kingtrim	Toronto, Ontario	<u>79</u>	<u>46</u>

*Island Phoenix commenced production July, 1989. Thunderbird was previously known as Harmac Woodroom #4. Somass and New Westminster were in the start-up phase during 1989.

MB's lumber products together with lumber purchased from other producers account for 71.6% of building materials segment sales and are essentially divided into appearance and construction grades. The range of appearance lumber products is concentrated in the western red cedar species of which the Company controls more than 10% of the world's resource. The cedar products are produced at the New Westminster, Canadian White Pine, and Somass mills. MB produces approximately 40 sizes and grades of green and kiln-dried bevel sidings, approximately 45 sizes and grades of green and dry channel sidings and tongue and groove products (suitable for wall paneling), and patio grades for decking and exposed beams. The producing mills for the Company's whitewood products include Alberni Pacific, Chemainus, Thunderbird, Powell River, and Island Phoenix which commenced production in July, 1989, largely directing its output to the local remanufacturing and export markets. The Chemainus mill specializes in producing a range of high valued products from high valued logs. The Alberni Pacific mill produces a wide variety of products for the Japanese housing market. Thunderbird and Pine Hill lumber continue to produce mostly dimension lumber for the U.S. market. The Company's Custom Processing Division buys whitewood lumber from the Company's mills and further processes it to meet the specifications of customers worldwide for uses such as European window frames and special Japanese decorative purposes.

The Parallam® plant in New Westminster commenced commercial production during 1988. Construction of a new Parallam® plant in Colbert, Georgia, is to be completed in early 1990 at a cost of U.S.\$63 million. Parallam®

parallel strand lumber is manufactured by bonding long strands of wood veneer into uniform structural beams, using a waterproof adhesive. It is made in a continuous process and cut to various lengths, in a wide range of cross-sectional sizes. In addition to its strength, the appearance and dimensional stability is facilitating its market acceptance by architects, engineers and builders in the residential and light commercial construction markets.

A wide range of panelboard products is presently produced at various mills across Western and Central Canada. Alberni Plywood produces softwood plywood products sold in a highly competitive market and has several value-added improved products. Standard plywood sold in the U.S. market is produced from pine logs at the Alabama mill. A specialty hardwood plywood plant at Nipigon produces such products as shafts for hockey sticks. Many of the Company's panelboard products are no longer cost competitive and the advisability of their continued production remains under review.

Capital expenditures in the building materials segment in 1989 amounted to \$246.8 million, compared to \$170.0 million and \$73.5 million in 1988 and 1987 respectively. During 1989, the construction of the Island Phoenix mill was completed at a cost of \$61 million, the new sawmill at Somass was completed at a cost of \$32 million and a new planer mill was completed at Alberni Pacific at a cost of \$14 million. During 1988, the construction of a gang quad sawmill at New Westminster was completed at a cost of \$14 million.

During 1989, U.S.\$74 million was approved for the construction of a new manufacturing plant near Deerwood, Minnesota with an annual capacity of 55 million net board feet of engineered, parallel strand lumber. The new technology compresses strands of wood into a dimensionally stable slab, which is then custom cut to customers' specifications and which is well suited to the door and window market. Construction will start in the spring of 1990.

Building Materials Marketing

The Company's marketing activities for building materials extend into most major world markets through sales offices and independent sales agents. In 1989 sales values were divided approximately as follows: 33.1% in Canada, 37.1% in the United States, 20.3% in Japan and the Orient and 9.5% elsewhere. The following table shows the distribution by market of MB's building materials sales in 1989, 1988 and 1987:

		Canada	United States	Japan & Orient	Europe & Other	Total
Lumber (MMfbm)	1989	417.3	994.3	247.1	155.1	1,813.8
	1988	401.2	1,081.9	241.5	165.8	1,890.4
	1987	398.0	1,090.5	215.4	179.4	1,883.3
Structural panelboards (MM sq.ft. 3/8")	1989	511.5	360.8	—	30.7	903.0
	1988	547.4	365.7	—	36.3	949.4
	1987	566.4	347.9	4.6	47.1	966.0

In the U.S. MB operates 19 distribution centres on the Atlantic coast, in the Mid-West, South and Pacific Northwest. In Canada its customers are serviced nation-wide by 22 distribution centres. MB has a lumber distribution company in Japan to market the high valued products demanded. Building materials sales offices in Hong Kong and Australia also market a full range of species and products oriented to regional preferences.

The markets in which MB sells its products are very competitive with a number of major companies competing in each market. Competition is on the basis of quality of product, price and service. Many of MB's products also compete with substitutes of various kinds. No material part of the business is dependent upon a single customer or small group of customers, although the Japanese market is the principal market for MB's high value white wood lumber products. Because of the time span and the wide diversity of specifications involved, it is not practicable to consolidate a back-order file.

PULP AND PAPER

MB operates pulp and paper mills at three locations in British Columbia — integrated pulp and newsprint mills at Powell River and at Port Alberni, and a pulp mill at Harmac. These mills manufacture newsprint and groundwood printing papers and bleached and unbleached kraft pulp. For the years ended December 31, 1989, 1988 and 1987 newsprint and groundwood printing papers accounted for 23.6%, 24.1% and 23.4% respectively of MB's consolidated sales values to unaffiliated customers while for market pulp the percentages were 14.1%, 12.7% and 11.6% respectively.

Pulp and Paper Facilities

MB operates the following facilities for the manufacture of pulp and paper products:

	Division	Location	Annual capacities at year-end 1989	1989 Production
Market Pulp (k-tonnes)	Harmac	Nanaimo, British Columbia	370	363
	Alberni Pulp and Paper	Port Alberni, British Columbia	80	77
	Powell River	Powell River, British Columbia	50	44
			<u>500</u>	<u>484</u>
Newsprint and Groundwood Printing Papers (k-tonnes)	Alberni Pulp and Paper	Port Alberni, British Columbia	355	356
	Powell River	Powell River, British Columbia	615	635
			<u>970</u>	<u>991</u>

Standard white newsprint is the Company's largest single paper product. Powell River currently has two machines manufacturing standard newsprint, two machines manufacturing groundwood printing papers and one machine which manufactures both products. A sixth newsprint machine, with an annual capacity of 65,000 tonnes was shut down in August, 1989 due to market conditions. Alberni has three machines, two which currently manufacture telephone directory and one which currently manufactures standard newsprint. The groundwood printing papers provide our customers with superior strength, opacity, smoothness, higher brightness and lighter weights. They are required for offset, rotogravure, and lithographic printing of publications such as Sunday magazines, newspaper advertising inserts and flyers, computer printout forms, and telephone and other directories.

The Company's main market pulp grade is bleached kraft softwood pulp manufactured at Harmac. Unbleached pulp is produced at Alberni and semi-bleached kraft pulp at Powell River.

Capital expenditures in the pulp and paper segment in 1989 amounted to \$194.5 million, compared to \$146.5 million and \$122.6 million in 1988 and 1987 respectively. Commentary on major additions during the last three years at each of the three mills follow. At Alberni, construction of a chemi-thermomechanical pulp line at a cost of \$100 million, a hydrogen peroxide bleaching plant at a cost of \$20 million, and a power boiler precipitator at a cost of \$18 million were completed during 1989; and the modernization of a standard newsprint machine to improve its paper quality was completed during 1988 at a cost of \$31 million. Expenditures are currently underway on a \$26 million new wrap line and management production system at Alberni and a \$35 million project to upgrade the Alberni #4 paper machine which includes the installation of a twin wire gap former and improved computerization which will improve product quality. In 1988 Powell River completed the \$70 million capital program announced in 1987 to improve product quality and increase production of specialty paper products. Powell River's expanded chemi-thermomechanical pulping and bleaching facilities became operational late in 1987. The twin wire refurbish of #9 paper machine was completed in mid-1988. The net result of these projects increased Powell River's annual paper capacity to 680,000 tonnes by mid-1988. In 1989, Powell River commenced a \$62 million project to increase the quality and quantity of standard newsprint from the mill's #10 paper machine. At Harmac, major capital spending has been directed at reducing air and water emissions. This includes the "lo-odour" project completed in 1988 at a cost of \$30 million, installation of a power boiler precipitator at a cost of \$14 million, replacement of a recovery boiler precipitator for \$7 million and a \$43 million project to reduce dioxins to non-traceable levels by the year 1991.

Pulp and Paper Marketing

MB pulp and newsprint is shipped worldwide. 77.5% of 1989 newsprint shipments were in North America while 84% of the pulp sales were to offshore markets. In its largest newsprint market, the western U.S. where MB supplies approximately one-sixth of the newsprint consumed, MB operates three offices. In 1988 MB concluded a marketing agreement with Alberta Newsprint Co. Ltd. of Whitecourt, Alberta. This new mill, which is scheduled to open in late 1990, will have a forecast annual capacity of 220,000 metric tonnes of standard newsprint. MB is committed to sell 84% of its production. MB also has sales offices in Tokyo, Hong Kong, Kuala Lumpur and Sydney to market pulp and newsprint in key, high-growth countries of the Pacific Rim and employs sales agents in other Pacific Rim markets. United Kingdom newsprint and groundwood paper customers are serviced from an office in London. European pulp markets are serviced from Brussels, and U.S. pulp customers from the Danbury, Connecticut office.

MB also markets pulp and paper products for others, particularly bleached softwood kraft pulp and lightweight coated papers from Koninklijke Nederlandse Papierfabrieken N.V. (KNP). The following table shows where MB's pulp and paper products were sold in 1989, 1988 and 1987:

		<u>Canada</u>	<u>United States</u>	<u>Japan & Orient</u>	<u>Europe</u>	<u>Other</u>	<u>Total</u>
Newsprint (k-tonnes)	1989	103.8	667.0	118.4	25.9	79.7	994.8
	1988	101.7	676.8	89.6	28.8	87.9	984.8
	1987	99.5	674.6	96.5	26.2	79.0	975.8
Market pulp (k-tonnes)	1989	13.5	67.1	133.0	245.9	43.8	503.3
	1988	14.8	64.1	123.6	239.7	47.6	489.8
	1987	14.6	67.3	128.0	228.1	57.9	495.9

Most of MB's pulp and newsprint shipments are covered by contracts which are subject to prices as announced from time to time. Contracts which may be firm as to quantity are not firm as to price and thus a meaningful figure for the value of contractual shipments is not possible. No material part of the business is dependent upon a single customer or small group of customers.

For the grades supplied, MB is fully competitive in major markets on quality, price and service. There are a number of pulp and paper suppliers in all of the major markets. MB does not have a dominant position in any market.

MB's newsprint mills are well situated on Canadian West Coast deep sea ports to assure its customers of a reliable, steady supply.

In 1989 through 1992 a large increase in North American newsprint capacity is occurring. This increased capacity has resulted in very strong price competition amongst suppliers in 1989 and is expected to continue through 1990. Current estimates of 1989 and 1990 capacity increases are 2.1% and 4.6% respectively, while in the ten year period ending 1987 newsprint consumption grew at approximately 3% per year. In 1988 and 1989 consumption grew at less than that historical rate.

CONTAINERBOARD AND PACKAGING

MB manufactures containerboard (linerboard and corrugating medium) at Pine Hill, Alabama, corrugating medium at Sturgeon Falls, Ontario, and corrugated containers in the United States. In 1989 containerboard sold outside the consolidated enterprise (linerboard and corrugating medium) accounted for 8.3% of consolidated sales values as compared to 8.4% in 1988 and 7.9% in 1987. For the years ended December 31, 1989, 1988 and 1987 corrugated containers accounted for 7.0%, 7.8% and 8.3% respectively of MB's consolidated sales values to unaffiliated customers.

Containerboard and Packaging Facilities

MB operates the following facilities for the manufacture of containerboard and packaging products:

	<u>Division</u>	<u>Location</u>	<u>Annual capacities at year-end 1989</u>	<u>1989 Production</u>
Linerboard (k-tonnes)	Pine Hill	Pine Hill, Alabama	400	400
Corrugating Medium (k-tonnes)	Pine Hill	Pine Hill, Alabama	233	224
	Sturgeon Falls	Sturgeon Falls, Ontario	71	70
			<u>704</u>	<u>694</u>
Corrugated Containers (k-tonnes)	10 Locations	United States	<u>336</u>	<u>250</u>

The Pine Hill mill produces a first-class corrugating medium and its linerboard machine is one of the industry's most efficient. The mill's testing laboratory continues to ensure consistently high quality, and upgrading equipment will further improve quality. The U.S. corrugated container plants, located in nine states between New York and Texas, produce and sell products ranging from bulk-bin industrial boxes to small custom-design display packaging. These plants also have a significant portion of the U.S. lamp wrap market.

Capital expenditures in the containerboard and packaging segment in 1989 amounted to \$59.4 million compared to \$32.8 million and \$19.5 million in 1988 and 1987 respectively. In 1988, MB approved U.S.\$17 million for phase II of a program which had commenced in 1987 to enhance the quality of Pine Hill's linerboard. In early 1989, a further U.S.\$62 million was approved for phase III of the project. In addition to quality enhancements, annual capacity will increase by 70,000 tons. At December 31, 1989 U.S.\$14.6 million had been spent on phases II and III.

Certain Alabama facilities and equipment at two United States corrugated container plants are leased with options to purchase at nominal amounts. All other containerboard and packaging manufacturing facilities are owned by MB.

Containerboard and Packaging Marketing

A substantial amount of the linerboard and corrugating medium sold by the Pine Hill, Alabama mill is utilized by MB's packaging operations in the United States. Pine Hill also sells linerboard to affiliated corrugated container plants in Canada and the United Kingdom (see Investment Section). The corrugating medium sold by Sturgeon Falls, Ontario is mainly utilized by affiliated Canadian corrugated container plants (see Investment Section). The large number of producers of containerboard in North America and offshore compete on the basis of quality, price and service. There are no material backlog sales to unaffiliated customers. The following table shows where MB's containerboard and corrugated containers were sold in 1989, 1988 and 1987:

		Canada	United States	Japan & Orient	Europe & Other	Total
Containerboard (k-tonnes)	1989	73.8	375.2		82.8	531.8
	1988	72.6	367.1		72.6	512.3
	1987	80.1	329.2	4.1	75.3	488.7
Corrugated Containers (k-tonnes)	1989		245.8			245.8
	1988		266.9			266.9
	1987		278.4		.2	278.6

The manufacture and marketing of corrugated containers is a specialized regional business. Custom design of corrugated containers is part of MB's marketing services provided through sales offices at plant locations or division headquarters. The market for these products is highly competitive, with competition on the basis of service, quality and price. Information on the dollar value of order backlogs is not aggregated for corrugated containers.

FOREIGN EXCHANGE

MB's export sales are principally denominated in United States dollars. Any significant change in the Canadian dollar against the U.S. dollar has a significant effect on Canadian dollar amounts realized.

If the U.S. dollar is weaker against other foreign producer currencies, prices quoted in U.S. dollars can be substantially increased in those countries having strong currencies. New opportunities for export arise in those markets as traditional suppliers with strong currencies have a competitive disadvantage. However, when the U.S. dollar is very strong relative to a number of foreign currencies, prices quoted in U.S. dollars fall, traditional North American markets become more competitive as a result of foreign penetration, and foreign markets are considerably less profitable.

OTHER

This segment of MB's business consists mainly of its transportation operations which are not related to the movement of MB forest products. (Transportation related to the movement of MB forest products is allocated to product segments for reporting purposes).

Transportation

MB's policy is to control through long term charters, a fleet of vessels capable of transporting to market approximately one-half of MB's forest products volume shipped by sea. MB currently has six vessels, totalling approximately 230,000 deadweight tonnes under charter for initial periods in excess of one year. All are designed for the carriage of forest products, but can also be used to transport containers, general freight and dry bulk commodities. While these vessels are principally engaged in the carriage of MB forest products, they also carry

forest products for other shippers and participate in steel, container and general freight back-haul trades in order to minimize empty steaming.

Remaining MB deep sea freighting requirements are met through a combination of spot charters, short term charters and contracts of affreightment with independent shipping companies.

To meet other freighting requirements, MB contracts with Canadian and U.S. railroads and trucking firms for varying periods. MB also operates a barge system on the Pacific coast for transporting newsprint to California and a fleet of tugs, barges and log carriers which are used primarily between logging divisions and mill storage grounds in British Columbia.

INVESTMENTS

MB has investments in various companies to provide steady markets for its products manufactured in North America and to achieve a degree of geographic and product diversification complementary to its North American base.

Investment in Partly-Owned Companies

As at December 31, 1989 investments in partly-owned companies were carried in the financial statements at a value of \$380.4 million.

The most significant investment is in Koninklijke Nederlandse Papierfabrieken N.V. (KNP), a Dutch public company with headquarters in the Netherlands. On January 3, 1989, KNP acquired an interest of approximately 50% in the major Austrian fine paper company Leykam-Mürztaler. On that same date MacMillan Bloedel subscribed and paid for an additional 5% common share interest in KNP at a cost of \$46.7 million. KNP also issued another 5% common share interest to the previous owners of Leykam-Mürztaler as part of the acquisition. KNP also has 50% interests in RP Europa B.V., producer of paper for corrugated board and Hch Sieger GmbH & Co. KG, producer of paper for corrugated board and corrugated board. At December 31, 1989 MacMillan Bloedel's shareholding in KNP stood at 28%. KNP is a major producer of coated and uncoated specialty printing paper in the European Economic Community. KNP owns and operates three paper mills in the Netherlands and one in Belgium, with an annual aggregate productive capacity of 780,000 tonnes and purchases pulp from MB. As at December 31, 1989 KNP also had packaging facilities with an annual capacity of 520,000 tonnes (reduced to 440,000 tonnes on January 1, 1990 with the sale of KNP Vouwkarton B.V. to a joint venture) of paperboard and packaging material and 80,000 tonnes of corrugated cases.

The Company has a 50% partnership interest in Island Paper Mills (IPM), at New Westminster, British Columbia. IPM is a fine paper mill in Western Canada and produces a broad range of uncoated free sheet grades. At December 31, 1989 the aggregate annual capacity was 114,000 tonnes. During 1988, IPM commenced construction of an off-machine coater. The \$82 million project is expected to be completed in April, 1990.

The Company has a 50% interest in MacMillan Bathurst Inc., which is one of Canada's largest corrugated container manufacturing companies owning 13 corrugated container plants widespread throughout Canada. At December 31, 1989 these plants had an annual productive capacity of 425,000 tonnes of corrugated containers.

MB owns 50% of MacMillan Smurfit SCA Limited (UK Corrugated). UK Corrugated ranks as the third largest producer of corrugated containers in the United Kingdom and at December 31, 1989 owned 10 corrugator plants and 3 sheet plants having an annual capacity of 240,000 tonnes of corrugated containers.

CAPITAL EXPENDITURE PROGRAM

Over the past five years MB's capital expenditures totalled \$1,335.6 million, with major expansions and modernizations completed at several locations. Of the \$518.4 million incurred in 1989, \$267.0 million were non-discretionary projects such as environmental projects, logging roads and routine maintenance of business capital. (Major discretionary capital expenditures are described in the facilities section of each industry segment and Note 4 of the consolidated financial statements.)

The following table summarizes consolidated capital expenditures by business segment over the past five years:

	1989	1988	1987	1986	1985	Total
	(\$ millions)					
Building materials	\$246.8	\$170.0	\$ 73.5	\$ 47.3	\$ 40.7	\$ 578.3
Pulp and paper	194.5	146.5	122.6	32.1	32.8	528.5
Containerboard and packaging	59.4	32.8	19.5	14.3	18.2	144.2
Other	17.7	14.7	41.0	6.3	4.9	84.6
	<u>\$518.4</u>	<u>\$364.0</u>	<u>\$256.6</u>	<u>\$100.0</u>	<u>\$ 96.6</u>	<u>\$1,335.6</u>

RESEARCH AND DEVELOPMENT

During the past three years MB spent the following on research and development programs aimed at development of new processes and products, greater utilization of timber resources, technical improvements to existing processes and products, and improved methods of silviculture and environmental protection:

	1989	1988	1987
	(\$ millions)		
Gross expenditures	\$23.3	\$21.6	\$16.6
Less: government grants .....	.8	1.2	1.3
Less: investment tax credits	3.9	3.8	4.1
Net	<u>\$18.6</u>	<u>\$16.6</u>	<u>\$11.2</u>

Of the 148 employees engaged in research in Canada, 115 professional (1988 — 110), technical and support staff are located at MB's Research and Development Centre in Burnaby, British Columbia. During 1989, the Company consolidated its research and development facilities in a building acquired in 1987. The total cost of purchasing the land and building and refurbishing the building was \$16.4 million.

HUMAN RESOURCES

At December 31, 1989, MacMillan Bloedel had approximately 12,000 employees in Canada, 3,000 in the United States of America and 100 elsewhere.

In British Columbia, 4,600 employees work in logging, lumber, plywood and particleboard operations and are represented by the IWA-Canada. 3,700 are employed in the Company's pulp and paper mills in British Columbia and are represented by the Canadian Paperworkers Union or the Pulp, Paper, and Woodworkers of Canada. The collective agreements with these Unions run from mid-1988 to mid-1991 and provide for a general wage increase of 5.5% in each of the last two years.

Alabama has the largest group of employees outside British Columbia and 800 of these are represented by the United Paperworkers International Union. A four year contract, covering lumber and plywood manufacture, is in its third year and provides for a 2% increase in each of the third and fourth years. The logging operations are in the third year of a three year contract with a wage increase of 2% in the final year. Linerboard and corrugated medium operations are in the second year of a four year contract with wage increases of 2.5% in the second and third years and 2% in the fourth year.

In the five years ended December 31, 1989, approximately 4.4% of total available hours of MB's British Columbia operations were lost due to labour disputes. Available hours lost in each of 1989, 1988 and 1987 averaged less than .4%.

ENVIRONMENT

In common with other companies in the forest products industry, the operations of MB are subject to various environmental protection laws and regulations. As a result of MB's attention to environmental protection, many measures had been instituted prior to the introduction of the present regulatory standards. Nevertheless, the evolving laws and regulations have required MB to undertake the installation of additional environmental control facilities.

During 1989, the Board of Directors established a committee to oversee the Company's environmental program on behalf of the Board.

In 1989, MB announced expenditures of \$75 million on equipment at its Harmac and Powell River mills to effectively eliminate the production of unwanted by-products, dioxins and furans. Current plans for other environmental control capital expenditures in 1990 are approximately \$62 million.

In January 1990, MB wrote to employees of the Alberni kraft pulp mill informing them that for the mill to meet the new environmental regulations relating to dioxins and chlorinated organics would cost approximately \$120 million. The Alberni kraft mill is old and small (500 tonnes per day) by today's standards and the required expenditure of \$120 million would do little to improve the capacity or productivity of the mill. The economics of the mill when faced with an additional capital cost of \$120 million are not satisfactory (the added interest and principal cost of this is over \$100 per tonne without continuing maintenance and operating costs). The Alberni Region also faces attacks on its tree-farm licence by special interest groups and Native Indians. This added uncertainty makes it likely that the kraft pulp mill will close prior to the proposed regulations becoming effective on January 1, 1992.

MB made capital expenditures of approximately \$38 million in 1989 to meet its legal commitments on environmental protection. In addition to this, approximately \$17 million was spent to operate and maintain the environmental controls already in place.

ENERGY

MB utilizes wood waste, spent liquors, electric power, petroleum products and, to a lesser extent, natural gas as energy sources in its manufacturing processes. In recent years approximately one-third of the electricity consumed by the Company in British Columbia is self-generated while in Alabama the figure is approximately 90%. Approximately 75% of the heat required in MB's manufacturing processes is generated from the burning of waste materials from its manufacturing operations. The balance of the energy and fuel requirements of the manufacturing operations has historically been purchased principally on a long term contract basis and partly on a spot basis from sources which MB believes to be reliable.

DIVIDENDS AND SHAREHOLDER INFORMATION

During the two years ended December 31, 1989, the Company declared the following dividends:

	1989	1988
	(\$ millions)	
Class B Preferred shares		
Series 4	1.8	1.8
Series 6	—	1.1
Series 8	4.5	4.6
Series 9	4.1	4.2
Series 10	5.2	5.2
Common shares	82.1	92.4

In 1989 and 1988 all dividends on Common shares were paid in cash. Preferred share dividends are paid quarterly.

The terms of issue of the Company's preferred shares prohibit the declaration or payment of any dividends, other than stock dividends in Common shares, unless all accrued dividends on such preferred shares have been paid or set apart for payment.

Cash dividends paid to United States shareholders of the Company's shares are subject to a 15% Canadian non-resident withholding tax.

Central Guaranty Trust Company (Vancouver, Calgary, Regina, Winnipeg, Toronto, Montreal) and The Chase Manhattan Bank (New York) are the Company's transfer agents and registrars.

29

3.14

309

22.5 234.99

Distribution of common shares and registered common shareholders as at February 1, 1990:

	Common shares	Common shareholders*
Canada	96,765,975	7,342
United States	5,859,893	753
Other	23,405	83
	<u>102,649,273</u>	<u>8,178</u>
Share warrants	552	
	<u>102,649,825</u>	

* Excluding approximately 18,000 beneficial shareholders, half of whom are employees of the Company.

Exchange listings:

Common shares listed: Toronto, Montreal, Vancouver.

Common shares quoted: NASDAQ.

Class B preferred share listings: Toronto, Montreal, Vancouver.

Ticker symbols: Canadian stock exchanges — MB; NASDAQ-MMBLF.

EXECUTIVE OFFICERS

<u>Name</u>	<u>Address</u>	<u>Age at Feb. 1 1990</u>	<u>Positions held during past five years</u>
A.H. Zimmerman.....	Toronto, Ontario	62	Chairman
C.C. Knudsen	Seattle, Washington	66	Vice-Chairman
R.V. Smith	West Vancouver, B.C.	63	President and Chief Executive Officer
D.L. McLauchlin	Vancouver, B.C.	63	Executive Vice-President since 1989; prior to which he was Executive Vice-President, Operations
R.B. Findlay	West Vancouver, B.C.	56	Senior Vice-President, Marketing since 1989; prior to which he was Senior Vice-President, Alberni Region
O.L. Forgacs	Vancouver, B.C.	59	Senior Vice-President, Research and Development
A.N. Grunder	North Vancouver, B.C.	53	Senior Vice-President, Finance and Administration since 1989; prior to which he was Vice-President, Information Systems & Services
J.L. Howard, Q.C.	Vancouver, B.C.	58	Senior Vice-President, Law & Corporate Affairs
J. St. C. Ross	West Vancouver, B.C.	58	Senior Vice-President, Regional Operations since 1989; prior to which he was Senior Vice-President, Nanaimo Region
W.W. Shorter	Montgomery, Alabama	57	Senior Vice-President, Containerboard and Packaging since 1989; and since 1978 has been President, MacMillan Bloedel Inc., indirectly a wholly owned subsidiary of the Company
R.N. Wiewel	West Vancouver, B.C.	62	Senior Vice-President, Product Development since 1989; prior to which he was Senior Vice-President, Marketing
G.A. Adams	West Vancouver, B.C.	51	Vice-President, Transportation
W.A. Adams	Nanaimo, B.C.	49	Vice-President, Nanaimo Region since 1989; prior to which he was President and Chief Executive Officer, Island Paper Mills
G.M. Ferguson	North Vancouver, B.C.	49	Vice-President, Treasurer
J.C. Finkbeiner	North Vancouver, B.C.	42	Vice-President, Tax, Properties and Risk Management

<u>Name</u>	<u>Address</u>	<u>Age at Feb. 1 1990</u>	<u>Positions held during past five years</u>
W.E. Hawkins	Richmond, B.C.	58	Vice-President, Engineering since 1985; prior to which he was General Manager, Engineering Services of the Company
G.H. Johncox	North Vancouver, B.C.	49	Vice-President, Human Resources since 1986; prior to which he was Vice-President, Industrial Relations of the Company
E. Lauritzen	West Vancouver, B.C.	51	Vice-President, Pulp & Paper Marketing
W.G. Low	Powell River, B.C.	59	Vice-President, Powell River Region since 1989; prior to which he was General Manager, Alberni Pulp and Paper, a division of the Company
R.V. Matthews	Vancouver, B.C.	46	Vice-President, Controller
F.H. Moonen	West Vancouver, B.C.	61	Vice-President, Government Affairs
D.W. St. John	Vancouver, B.C.	58	Vice-President, Lumber Marketing
A.C. Stubbs	North Vancouver, B.C.	45	Vice-President, Corporate Communications since 1988; prior to which he was Director, Public Relations of the Company
R.D. Tuckey	Port Alberni, B.C.	48	Vice-President, Alberni Region since 1989; prior to which he was General Manager, Harmac, a division of the Company
V.R. Worthy	West Vancouver, B.C.	52	Vice-President, Panelboards, Marketing Group
G.E. Mynett	Vancouver, B.C.	43	Corporate Secretary since 1989; prior to which he was Secretary and Solicitor since 1987; prior to which he was a Solicitor with the Company

SELECTED QUARTERLY FINANCIAL DATA

	1989				1988			
	Quarters				Quarters			
	I	II	III	IV	I	II	III	IV
	(\$ millions)							
Sales of products and services	807.0	862.0	818.0	786.7	796.5	851.5	824.4	801.1
Costs and expenses								
Materials, labour and operating expenses	618.2	668.7	639.5	634.6	574.3	632.3	641.1	604.1
Depreciation, depletion and amortization	31.0	33.5	32.3	33.6	31.8	30.9	29.4	32.5
Selling, general and administrative	50.9	55.7	53.9	56.7	48.2	56.4	50.1	54.4
	<u>700.1</u>	<u>757.9</u>	<u>725.7</u>	<u>724.9</u>	<u>654.3</u>	<u>719.6</u>	<u>720.6</u>	<u>691.0</u>
Operating earnings	106.9	104.1	92.3	61.8	142.2	131.9	103.8	110.1
Other income (expense)	2.1	2.4	.2	6.8	2.5	11.3	1.9	(24.8)
Interest expense	(11.2)	(13.3)	(14.0)	(15.1)	(11.3)	(11.2)	(10.8)	(10.2)
Earnings before income taxes	97.8	93.2	78.5	53.5	133.4	132.0	94.9	75.1
Income taxes	(39.4)	(38.7)	(24.0)	(21.4)	(54.9)	(50.6)	(36.7)	(19.2)
Earnings before undernoted items	58.4	54.5	54.5	32.1	78.5	81.4	58.2	55.9
Equity in earnings of partly-owned companies	15.0	13.8	10.9	7.5	13.1	13.1	12.3	17.3
Net earnings	73.4	68.3	65.4	39.6	91.6	94.5	70.5	73.2
Provision for dividends on preferred shares	(3.1)	(3.4)	(3.4)	(3.3)	(4.0)	(3.3)	(3.2)	(3.3)
Net earnings attributable to common shareholders	<u>70.3</u>	<u>64.9</u>	<u>62.0</u>	<u>36.3</u>	<u>87.6</u>	<u>91.2</u>	<u>67.3</u>	<u>69.9</u>
Net earnings per common share (dollars)								
basic .....	.68	.64	.60	.35	.85	.89	.66	.68
fully diluted .....	.66	.61	.59	.35	.82	.85	.64	.66
Price range of common shares on Toronto Stock Exchange (dollars)								
high	20.75	18.63	21.38	20.25	23.87	20.63	21.00	18.38
low	17.63	17.13	17.13	16.75	17.87	17.38	17.50	16.50
Dividends per common share (dollars)								
cash dividends .....	.20	.20	.20	.20	.15	.15	.20	.40

FIVE YEAR EARNINGS DATA

	1989	1988	1987	1986	1985
Sales (\$ millions)	<u>3,273.7</u>	<u>3,273.5</u>	<u>3,134.5</u>	<u>2,511.7</u>	<u>2,335.4</u>
Contributions to earnings (\$ millions)					
Building materials	139.1	186.8	206.4	83.3	44.5
Pulp and paper	180.8	254.9	229.6	141.9	70.7
Containerboard and packaging	113.6	118.0	88.9	19.7	8.1
Eliminations and unallocated items	(68.4)	(71.7)	(59.1)	(22.4)	(14.4)
Operating earnings	365.1	488.0	465.8	222.5	108.9
Other income (expense)	11.5	(9.1)	17.8	17.4	10.4
Interest expense	(53.6)	(43.5)	(50.7)	(67.3)	(92.0)
Earnings before income taxes	323.0	435.4	432.9	172.6	27.3
Income taxes	(123.5)	(161.4)	(183.8)	(65.5)	(8.5)
Equity earnings	<u>47.2</u>	<u>55.8</u>	<u>31.5</u>	<u>26.2</u>	<u>24.1</u>
Earnings before extraordinary item	246.7	329.8	280.6	133.3	42.9
Extraordinary item	—	—	—	45.0	—
Net earnings	246.7	329.8	280.6	178.3	42.9
Less: Provision for preferred dividends	13.2	13.8	21.3	33.5	26.6
Net earnings for common shareholders	<u>233.5</u>	<u>316.0</u>	<u>259.3</u>	<u>144.8</u>	<u>16.3</u>
Per common share (\$ per common share)					
Net earnings:					
before extraordinary item					
basic	2.27	3.08	2.56	1.07	.18
fully diluted	2.21	2.97	2.50	—	—
after extraordinary item					
basic	2.27	3.08	2.56	1.55	.18
fully diluted	2.21	2.97	2.50	—	—
Cash dividends on common shares .....	.80	.90	.82	.25	—
Stock dividends on common shares	—	—	—	—	.30

Notes:

- (1) The above data reflect the subdivision of each common share into three common shares on April 9, 1987.
- (2) Financial information is expressed in Canadian dollars. Canadian, U.S. dollar exchange rates as reported by the Bank of Canada were as follows:

	One Canadian dollar			
	High	Low	Average	Year-end
1989	US\$.8647	US\$.8286	US\$.8445	US\$.8637
1988 .....	.8433	.7700	.8124	.8384
1987 .....	.7714	.7255	.7541	.7692
1986 .....	.7332	.6950	.7197	.7244
1985 .....	.7575	.7141	.7325	.7156

MANAGEMENT'S DISCUSSION AND ANALYSIS RESULTS OF OPERATIONS

To assist the reader in this discussion, reference is made to Five Year Earnings Data on page 28 of this report.

COMPARISON OF 1989 AND 1988 EARNINGS

In 1989 MB recorded net earnings of \$246.7 million. This compares to the record 1988 net earnings of \$329.8 million. On a per common share basis, net earnings decreased from \$3.08 per common share in 1988 to \$2.27 per common share in 1989.

The major items contributing to the decrease were \$122.9 million decline in operating earnings, \$10.1 million increase in interest expense, and \$8.6 million decrease in equity earnings of partly-owned companies, partially offset by \$20.6 million increase in other income.

Sales of products and services were unchanged at \$3,273.7 million in 1989 compared with \$3,273.5 million in 1988. The following table provides an analysis of the change in key product sales from 1988 to 1989:

Product	Change in sales 1988 to 1989*	Change attributed to:	
		Volume	Price**
		(\$ millions)	
Pulp	\$ 41.3	\$ 10.6	\$ 30.7
Panelboards	13.5	(1.1)	14.6
Lumber .....	.2	(6.9)	7.1
Containerboard	(1.3)	10.2	(11.5)
Newsprint	(15.6)	11.2	(26.8)
Corrugated containers	(23.3)	(18.5)	(4.8)
Export logs	(39.3)	(42.1)	2.8
	(24.5)	<u>\$(36.6)</u>	<u>\$ 12.1</u>
Transportation services	9.0		
Other items	15.7		
Total	<u>\$.2</u>		

* Change in sales by product excludes freight.

** Including the effect of changing foreign currency exchange rates.

The \$122.9 million decrease in operating earnings is mainly attributable to increased production costs and the stronger Canadian dollar. On average, the Canadian dollar was approximately 4% stronger in 1989 than in 1988 which adversely affected net earnings by approximately \$28 million. Also contributing to the decline were lower prices for newsprint and containerboard and a reduction of export logs, partially offset by higher sales values for pulp and lumber, particularly value-added products, and higher shipment volumes of newsprint, pulp and containerboard.

Costs and expenses increased \$123.1 million reflecting a general increase in production costs as well as higher harvesting costs in B.C. Increased selling, general and administrative expenses largely reflect salary increases. Other income (expense) was a net expense in 1988 due to the loss on disposal of the Company's Thunder Bay waferboard facility and the write down of certain other facilities which were no longer cost competitive. Interest expense was higher in 1989 than 1988 due to higher borrowings.

Equity earnings declined \$8.6 million due to reduced earnings from all the Company's major investments.

BUILDING MATERIALS

MB's building materials segment's contribution to earnings decreased \$47.7 million from \$186.8 million in 1988 to \$139.1 million in 1989. Sales increased marginally by \$3.9 million from \$1,404.7 million in 1988 to \$1,408.6 million in 1989.

The following table shows sales and production of building materials products and the percentage of capacity utilization in each of the years 1989, 1988 and 1987:

	Sales		Production	
	Value (\$ millions)	Volume	Volume	Operating rate
1989				
Lumber (MMfbm)	\$1,008.6	1,814	792	78%
Plywood (MM sq.ft. 3/8")	142.5	479	240	71%
Waferboard (MM sq.ft. 3/8")	59.2	351	205	107%
Other	198.3			
	<u>\$1,408.6</u>			
1988				
Lumber (MMfbm)	\$1,008.1	1,890	925	84%
Plywood (MM sq.ft. 3/8")	124.2	453	265	78%
Waferboard (MM sq.ft. 3/8")	61.6	420	326	91%
Other	210.8			
	<u>\$1,404.7</u>			
1987				
Lumber (MMfbm)	\$1,022.2	1,883	1,059	90%
Plywood (MM sq.ft. 3/8")	134.1	455	312	93%
Waferboard (MM sq.ft. 3/8")	71.2	424	376	97%
Other	202.3			
	<u>\$1,429.8</u>			

1989 U.S. housing starts at 1.37 million again declined during the year, down from 1.49 million in 1988. The slow down in the North American economy which commenced in 1988 continued throughout 1989. 1989 softwood lumber consumption was lower in both the U.S. and Canada compared with 1988. A major and growing area of lumber consumption in today's market is in renovation and repairs, with commercial construction and industrial application also accounting for a large share.

Japanese housing starts in 1989 are estimated at 1.66 million, down slightly from 1.68 million in 1988. MB successfully continued its penetration into the high value-added Japanese market.

Sales volumes for wood products were lower in 1989 compared with 1988, but average lumber sales values were higher as a result of MB's continued improvement in lumber product mix due to the Company's commitment to value-added products. MB's purchases of dimension lumber were, however, higher in 1989 than in 1988 due to lower production, largely attributable to the closure of Harmac Woodroom #3 for replacement. The Japanese market significantly contributed to higher 1989 sales values for lumber compared with 1988 levels. The new Island Phoenix mill, which started up in July, 1989, is designed to produce grades and sizes particularly suited to Japan and other overseas markets, and to the local remanufacturing industry. This continues the Company's shift away from the U.S. dimension market by diversifying into various European and far eastern markets. The Chemainus and Somass mills are producing higher value-added products than in 1988.

MB's production of waferboard was lower in 1989 than in 1988 due to the closure of the Thunder Bay waferboard plant in November, 1988, although prices were up significantly.

Plywood and specialty board production was below 1989 mill capacities due to low sales volumes. The hardboard operation at Sturgeon Falls also operated at below capacity due to low sales volumes.

Parallam® has been included in this segment for the first time in 1989. During 1989, a further \$1.2 million was invested in the New Westminster plant to increase capacity. As a result, the plant is currently in a start-up mode.

PULP AND PAPER

MB's pulp and paper segment's contribution to earnings decreased \$74.1 million from \$254.9 million in 1988 to \$180.8 million in 1989. Sales increased by \$27.7 million from \$1,282.5 million in 1988 to \$1,310.2 million in 1989.

The following table shows sales and production of pulp and paper products and the percentage of capacity utilization in each of the years 1989, 1988 and 1987:

	Sales		Production	
	Value (\$ millions)	Volume k tonnes	Volume k tonnes	Operating rate
1989				
Newsprint — standard	\$ 413.1	579	575	
— specialty papers	358.8	416	416	
Total newsprint	771.9	995	991	98%
Market pulp	460.5	503	484	97%
Other	77.8			
	<u>\$1,310.2</u>			
1988				
Newsprint — standard	\$ 443.8	592	600	
— specialty papers	343.6	393	393	
Total newsprint	787.4	985	993	96%
Market pulp	416.2	490	480	97%
Other	78.9			
	<u>\$1,282.5</u>			
1987				
Newsprint — standard	\$ 430.7	611	582	
— specialty papers	304.2	365	365	
Total newsprint	734.9	976	947	99%
Market pulp	364.2	496	482	100%
Other	46.2			
	<u>\$1,145.3</u>			

U.S. newsprint consumption in 1989 was slightly lower than 1988 levels, but shipments declined more than consumption because publishers' inventories, which had built up in 1988 were reduced during 1989. MB's shipment volumes were lower for standard newsprint, but were more than offset by higher volumes for specialty papers. Prices were lower for both newsprint and specialty papers. The Company discounted newsprint prices during 1989 in order to meet competitive prices and to maintain its market share. Due to increasingly competitive markets arising from significant new capacity additions in 1989 and 1990 and because of high mid-year newsprint inventories, the Company shut down its number 8 newsprint machine at Powell River in August. The Canadian Pulp and Paper Association shows a total North American net increase in capacity during 1989 and 1990 of 2.1% (325,000 tonnes) and 4.6% (730,000 tonnes) respectively. North American newsprint consumption averaged 3% annual growth in the period 1977-1987. However, there was little or no growth in consumption in 1988 and 1989. World wide newsprint capacity to be added during 1990 is 1,395,000 tonnes.

The Company will continue to emphasize sales to quality North American accounts and serve export markets in 1990.

The table below lists newsprint selling prices in the key U.S. market in 1988 and 1989:

(U.S.\$)	1989	1988
Standard News		
List price (per tonne) (Note 1)	\$630 less 5%	\$630 less 5%
Groundwood Printing Papers		
Average gross sales value (per tonne) (Note 2)	\$755	\$721*

Notes:

(1) Contract Performance Incentive Program discount of 5% became effective July 1983. Additional discounts averaging 4% in 1988 and 6% in 1989 have been negotiated to maintain competitive pricing.

(2) Average gross sales value is the weighted average selling price for all groundwood printing paper grades sold in the year.

* Restated.

The strong pulp market of the previous three years continued throughout 1989 and pulp was again a major contributor to operating earnings. MB's pulp shipments were higher in 1989 compared with 1988 due to the strong market, the 1988 closure of the Harmac pulp mill for five weeks to complete a capital project and an illegal strike at Powell River. Inventories remain at low levels.

The table below lists selling prices for northern bleached softwood kraft pulp in MB's key markets for 1988 and 1989:

(U.S.\$)	1989		1988			
	Quarters		Quarters			
	I	II-IV	I	II	III	IV
Europe	\$810	\$840	\$680	\$720	\$760	\$760
U.S.A.	\$800	\$830	\$655	\$695	\$735	\$760
Japan	\$810	\$840	\$680	\$720	\$760	\$760

Newly evolving environmental regulations governing air and water emissions will be costly to comply with and are causing the long term economic viability of certain of MB's relatively older and smaller mills to be severely questioned. In January, 1990 the employees were informed that MB is unlikely to make the necessary capital expenditure (approximately \$120 million) to have the small kraft pulp mill in Alberni comply with evolving environmental regulations. Such an expenditure would do little to make the small mill more productive. Consequently it is likely that the Alberni kraft pulp operation will shut down before January 1, 1992, the date the proposed regulations become effective.

The Company's major pulp and paper operating facilities continue to be monitored closely and funds are being committed to these profitable operations to meet evolving environmental regulations.

CONTAINERBOARD AND PACKAGING

MB's containerboard and packaging segment's contribution to earnings decreased \$4.4 million from \$118.0 million in 1988 to \$113.6 million in 1989. Sales decreased by \$26.0 million from \$530.1 million in 1988 to \$504.1 million in 1989.

The following table shows sales and production of containerboard and packaging products and the percentage of capacity utilization in each of the years 1989, 1988 and 1987:

	Sales (outside MB)		Production	
	Value (\$ millions)	Volume k tonnes	Volume k tonnes	Operating rate
1989				
Linerboard	\$158.4	305	400	100%
Corrugating medium	<u>114.9</u>	<u>226</u>	<u>294</u>	97%
Total containerboard	273.3	531	694	99%
Corrugated containers	230.3	246	250	74%
Other	<u>.5</u>			
	<u>\$504.1</u>			
1988				
Linerboard	\$155.8	283	397	104%
Corrugating medium	<u>118.6</u>	<u>229</u>	<u>302</u>	102%
Total containerboard	274.4	512	699	103%
Corrugated containers	254.6	267	268	87%
Other	<u>1.1</u>			
	<u>\$530.1</u>			

	Sales (outside MB)		Production	
	Value (\$ millions)	Volume k tonnes	Volume k tonnes	Operating rate
1987				
Linerboard	\$141.1	272	387	104%
Corrugating medium	105.0	217	294	99%
Total containerboard	246.1	489	681	102%
Corrugated containers	258.8	279	278	96%
Other	1.2			
	<u>\$506.1</u>			

Sales volumes of linerboard were higher in 1989 than in 1988. In the first quarter of 1988 linerboard prices increased in the U.S. by U.S.\$30 per ton to U.S.\$410 per ton where they remained during 1989. However, price discounting occurred on linerboard and medium in both the U.S. and U.K. markets.

A significant portion of Pine Hill's containerboard is sold to its affiliated U.S. corrugated container plants. 1989 U.S. corrugated box sales and prices were lower than in 1988 and continued to show erosion in the latter part of the year indicating further competitive pricing pressures.

EARNINGS SENSITIVITIES

MB's earnings are sensitive to fluctuations in prices for its products and in currency exchange rates. Based on production in 1989, a Cdn.\$10 per unit change in the average net sales prices of its principal products or a \$.01 change in the value of the Canadian dollar relative to \$1.00 U.S. effect MB's annualized after tax earnings approximately as follows:

	Approximate annual effect on net earnings (\$ millions)
Price sensitivity	
Lumber \$10 change per Mfbm	\$5
Newsprint and specialty papers \$10 change per tonne	6
Containerboard \$10 change per tonne	4
Pulp \$10 change per tonne	3
Exchange sensitivity	
Canadian dollar — change of \$.01 Canadian relative to \$1.00 U.S.	6

COMPARISON OF 1988 AND 1987 EARNINGS

In 1988 MB achieved record net earnings of \$329.8 million. This compares to 1987 earnings of \$280.6 million. On a per common share basis, net earnings increased from \$2.56 per common share in 1987 to \$3.08 per common share in 1988. Sales of products and services increased 4.4% to \$3,273.5 million in 1988 from \$3,134.5 million in 1987.

The major items contributing to the increased earnings were \$22.2 million in operating earnings and \$24.3 million in equity earnings of partly-owned companies.

The \$22.2 million increase in operating earnings was mainly attributable to higher prices for all products except panelboards and higher shipment volumes for containerboard and newsprint. However, the stronger Canadian dollar decreased realizations from U.S. dollar denominated sales partially offsetting price increases. An appreciation in the Canadian dollar relative to the U.S. dollar of approximately 8% over the average of the previous year adversely impacted earnings by approximately \$110 million before income taxes.

MB's building materials segment's contribution to earnings decreased \$19.6 million largely due to lower sales volumes for most wood products. However, MB's average lumber sales values were higher in 1988 than in 1987 due to value-added products. The 1987 15% export charge on softwood lumber shipped from Canada to the United States of approximately \$26.9 million was largely replaced in 1988 by higher stumpage and royalty payments of approximately \$10.0 million and reforestation costs of approximately \$12.0 million.

The pulp and paper segment's contribution to earnings increased \$25.3 million due to higher prices for all products and higher sales volumes of specialty paper, slightly offset by lower sales volumes of standard newsprint.

The strong pulp market continued throughout 1988, but MB's shipments were slightly lower compared with 1987 due to the closure of Harmac pulp mill for five weeks to complete a capital project and an illegal strike at Powell River.

The containerboard and packaging segment's contribution to earnings increased \$29.1 million, mainly due to higher containerboard sales volumes and prices. Corrugated container volumes were lower, but prices were higher.

Costs and expenses increased \$116.8 million principally reflecting increased production costs as a result of higher wage rates and increased logging costs. Increased selling, general and administrative expenses largely reflect salary increases. The loss on disposal of the Company's Thunder Bay waferboard facility together with the write down of certain other facilities which were no longer cost competitive was charged to other income and expense resulting in a net expense of \$9.1 million for 1988. The provision for preferred dividends was \$7.5 million lower in 1988 than 1987 reflecting the significant reduction in preferred shares which mainly occurred in the first half of 1987.

The \$24.3 million increase in equity earnings was primarily due to the strength of the MB's investment in KNP where production and European fine paper markets have been excellent.

FINANCIAL POSITION

MB accesses the world's major financial markets and, in order to obtain the most advantageous terms of credit, maintains a flexible financial structure. MB's policy in respect of debt leverage is to maintain a ratio of debt to invested capital of 25% or less at the top of the business cycle and no more than 35% at the bottom of the business cycle.

At December 31, 1989, interest-bearing debt and redeemable term preferred shares as a ratio to invested capital was 27.0% compared to 18.9% at the end of 1988.

As at December 31, 1989, MB's borrowing capacity was as follows:

	Available	Utilized
	(\$ millions)	
Short term lines of credit	\$ 287.8	\$ 70.3
Long term lines of credit	650.0	—
	937.8	70.3
Authorized short term commercial paper	500.0	42.0
	<u>\$1,437.8</u>	<u>\$112.3</u>

During October, 1989, the Company received Cdn.\$118.0 million from a 215,000,000 Dutch guilder loan at an interest rate of 8.1% maturing October, 1996, and during December, 1989 the Company received Cdn.\$232.7 million from a U.S.\$200 million loan at an interest rate of 9.2% maturing December, 1999. The net proceeds were used to repay short term debt, finance capital expenditures and for other general corporate purposes. At December 31, 1989 total interest-bearing indebtedness including the convertible subordinated debentures amounted to \$909.0 million, up from the \$580.1 million at December 31, 1988.

Funds generated by operations in 1989 amounted to \$555.1 million (1988 — \$592.9 million) with net funds required of \$304.3 million (1988 — \$45.5 million) after capital expenditures and investments of \$594.8 million (1988 — \$388.9 million), payment of preferred dividends, interest and taxes of \$182.5 million (1988 — \$157.1 million), and payment of common share dividends of \$82.1 million (1988 — \$92.4 million).

Capital expenditures in 1989 on property, plant and equipment were \$518.4 million of which \$267.0 million related to ongoing environmental and safety items and the replacement of existing capacity and technological updating. Details of specific capital expenditures have been described in each segment's section where the business of MB has been discussed.

In 1989, the Company paid cash dividends on its common shares amounting to \$.80 per share.

FIVE YEAR FINANCIAL DATA

	1989	1988	1987 (\$ millions)	1986	1985
Funds generated by operations	555.1	592.9	554.2	404.5	247.9
Depreciation, depletion and amortization	130.4	124.6	127.4	105.4	114.7
Capital expenditures	518.4	364.0	256.6	100.0	96.6
Interest paid	51.7	44.9	52.9	67.1	91.6
Preferred share dividends paid	15.6	16.9	26.1	35.5	26.5
Common share dividends paid	82.1	92.4	82.8	23.3	.2
Current assets	967.3	932.0	875.7	683.2	733.1
Current operating liabilities	389.0	374.7	313.1	229.6	239.5
Operating working capital	578.3	557.3	562.6	453.6	493.6
Property, plant and equipment	1,869.6	1,504.4	1,350.6	1,258.6	1,317.2
Investments and other assets	421.2	316.7	289.5	254.1	269.9
Net assets employed	2,869.1	2,378.4	2,202.7	1,966.3	2,080.7
Short term interest-bearing debt	79.0	67.6	13.3	55.9	63.1
Current portion of long term debt	18.8	12.0	13.7	39.1	25.5
Long term debt	661.2	350.5	398.8	452.3	775.1
Interest-bearing debt (excluding convertible subordinated debentures)	759.0	430.1	425.8	547.3	863.7
Convertible subordinated debentures	150.0	150.0	150.0	—	—
Redeemable term preferred shares	17.0	19.0	72.3	214.6	218.3
Redeemable convertible preferred shares	—	—	—	50.1	95.9
Other redeemable preferred shares	106.5	108.9	109.4	110.0	50.0
Common equity	1,509.1	1,376.4	1,194.3	945.7	761.9
Deferred credits	327.5	294.0	250.9	98.6	90.9
Total invested capital (Note 3)	2,869.1	2,378.4	2,202.7	1,966.3	2,080.7
Total assets (Note 4)	3,258.1	2,753.1	2,515.8	2,195.9	2,320.2
Total long term debt, convertible subordinated debentures and redeemable preferred shares	934.7	628.4	730.5	827.0	1,139.3
Interest-bearing debt (excluding convertible subordinated debentures) as a percentage of invested capital	26.5%	18.1%	19.3%	27.8%	41.5%
Interest-bearing debt (excluding convertible subordinated debentures) and redeemable term preferred shares as a percentage of invested capital	27.0%	18.9%	22.6%	38.7%	52.0%

Notes:

- (1) The conversion of \$43.0 million of redeemable convertible preferred shares into common shares in January 1987 has been given effect as at December 31, 1986 in the above table.
- (2) For a summary of U.S. and Canadian dollar exchange rates see Note 2 accompanying five year earnings data on page 28 of this report.
- (3) "Invested capital" is defined as the sum of interest-bearing debt, convertible subordinated debentures, deferred income taxes, deferred revenue and shareholders' equity.
- (4) Prior years have been restated to conform with the presentation in 1989.

MacMILLAN BLOEDEL LIMITED
Consolidated Statements of Financial Position
Net Assets Employed

	December 31	
	1989	1988*
	(\$ millions)	
Current assets:		
Short term investments and deposits	\$ 47.9	\$ 25.0
Accounts receivable —		
Trade	354.0	361.2
Other	36.3	40.5
Inventories (Note 2)	526.1	499.7
Prepaid expenses	3.0	5.6
	<u>967.3</u>	<u>932.0</u>
Deduct current liabilities (excluding interest-bearing debt):		
Bank overdrafts in excess of cash in banks	17.6	19.8
Trade accounts payable	160.3	156.2
Accrued payroll and related liabilities	129.6	120.5
Accrued interest on borrowed funds	16.4	14.5
Other accounts payable and accrued liabilities	80.5	50.4
Income taxes payable (recoverable)	(15.4)	13.3
	<u>389.0</u>	<u>374.7</u>
Operating working capital	<u>578.3</u>	<u>557.3</u>
Investments and other assets:		
Investments accounted for by the equity method (Note 3)	380.4	276.4
Other investments and assets, at cost	40.8	40.3
	<u>421.2</u>	<u>316.7</u>
Property, plant and equipment: (Note 4)		
Buildings and equipment	2,744.4	2,367.2
Less: Accumulated depreciation	1,202.8	1,133.9
	1,541.6	1,233.3
Construction in progress	140.9	103.7
	1,682.5	1,337.0
Timber and land less accumulated depletion	200.1	164.2
Logging roads	12.9	12.4
Foreign exchange translation adjustment	(25.9)	(9.2)
	<u>1,869.6</u>	<u>1,504.4</u>
	<u>\$2,869.1</u>	<u>\$2,378.4</u>

*Certain 1988 amounts have been reclassified to conform with the presentation in 1989.

Approved by the Board:

R.V. Smith,
Director

A.H. Zimmerman,
Director

MacMILLAN BLOEDEL LIMITED

Consolidated Statements of Financial Position

Invested Capital

	December 31	
	1989	1988
	(\$ millions)	
Short term interest-bearing debt:		
Bank indebtedness (Note 5)	\$ 37.0	\$ 42.7
Notes payable	42.0	24.9
Current portion of long term debt (Note 6)	18.8	12.0
	<u>97.8</u>	<u>79.6</u>
Long term obligations:		
Term loans (Note 7)	478.7	169.1
Notes, bonds and debentures (Note 8)	176.8	177.6
Other	30.3	36.7
Foreign exchange translation adjustment	(17.6)	(23.4)
	<u>668.2</u>	<u>360.0</u>
Deferred income taxes	320.5	284.5
	<u>1,086.5</u>	<u>724.1</u>
Convertible Debentures and Shareholders' Equity:		
Convertible subordinated debentures (Note 9)	150.0	150.0
Shareholders' equity		
Share capital: (Note 10)		
Preferred shares	123.5	127.9
Common shares	552.0	552.0
	<u>675.5</u>	<u>679.9</u>
Retained earnings	1,023.3	874.6
	<u>1,698.8</u>	<u>1,554.5</u>
Foreign exchange translation adjustment	(66.2)	(50.2)
Shareholders' equity	<u>1,632.6</u>	<u>1,504.3</u>
	<u>1,782.6</u>	<u>1,654.3</u>
Commitments (Notes 10 and 11)		
	<u>\$2,869.1</u>	<u>\$2,378.4</u>

MacMILLAN BLOEDEL LIMITED

Consolidated Statements of Earnings

	Year ended December 31		
	1989	1988	1987
	(\$ millions)		
Sales of products and services	\$3,273.7	\$3,273.5	\$3,134.5
Costs and expenses:			
Materials, labour and other operating expenses	2,561.0	2,451.8	2,350.1
Depreciation, depletion and amortization	130.4	124.6	127.4
Selling, general and administrative	217.2	209.1	191.2
	<u>2,908.6</u>	<u>2,785.5</u>	<u>2,668.7</u>
Operating earnings	365.1	488.0	465.8
Other income (expense)	11.5	(9.1)	17.8
Interest expense	(53.6)	(43.5)	(50.7)
Earnings before income taxes	<u>323.0</u>	<u>435.4</u>	<u>432.9</u>
Income taxes:			
Current	90.4	133.3	47.3
Deferred	33.1	28.1	136.5
	<u>123.5</u>	<u>161.4</u>	<u>183.8</u>
Earnings before undernoted item	199.5	274.0	249.1
Equity in earnings of partly-owned companies	47.2	55.8	31.5
Net earnings	246.7	329.8	280.6
Provision for dividends on preferred shares	13.2	13.8	21.3
Net earnings attributable to common shareholders	<u>\$ 233.5</u>	<u>\$ 316.0</u>	<u>\$ 259.3</u>
Earnings per common share (dollars)			
Basic	<u>\$ 2.27</u>	<u>\$ 3.08</u>	<u>\$ 2.56</u>
Fully diluted	<u>\$ 2.21</u>	<u>\$ 2.97</u>	<u>\$ 2.50</u>

MacMILLAN BLOEDEL LIMITED

Consolidated Statements of Changes in Financial Position

	Year ended December 31		
	1989	1988	1987
	(\$ millions)		
Internal funds:			
Generated by operations			
Operating earnings	\$ 365.1	\$488.0	\$ 465.8
Depreciation, depletion and amortization	130.4	124.6	127.4
Other income	11.5	20.0	17.8
Dividends from partly-owned companies	17.2	14.2	10.9
Decrease (increase) in operating working capital			
Receivables	11.4	(53.1)	(77.6)
Inventories	(26.4)	(55.7)	(61.0)
Other	45.9	54.9	70.9
Generated by operations	<u>555.1</u>	<u>592.9</u>	<u>554.2</u>
Required for:			
Interest	51.7	44.9	52.9
Dividends to preferred shareholders	15.6	16.9	26.1
Income taxes currently paid	115.2	95.3	23.1
	<u>182.5</u>	<u>157.1</u>	<u>102.1</u>
Net internal funds	<u>372.6</u>	<u>435.8</u>	<u>452.1</u>
Funds invested long term:			
Capital expenditures	518.4	364.0	256.6
Investments and other assets	76.4	24.9	32.6
	<u>594.8</u>	<u>388.9</u>	<u>289.2</u>
	(222.2)	46.9	162.9
Dividends to common shareholders	82.1	92.4	82.8
Funds generated (required)	<u>(304.3)</u>	<u>(45.5)</u>	<u>80.1</u>
Financing transactions:			
Issue of convertible subordinated debentures	—	—	150.0
Retraction and redemption of preferred shares	(4.0)	(52.0)	(137.5)
Net interest-bearing debt incurred (repaid)	327.0	40.8	(110.8)
Issue of common shares	—	4.4	16.6
Disposal of investments, subsidiaries and other	6.4	(3.5)	43.2
Financing provided (repaid)	<u>329.4</u>	<u>(10.3)</u>	<u>(38.5)</u>
Increase (decrease) in funds*	<u>\$ 25.1</u>	<u>\$ (55.8)</u>	<u>\$ 41.6</u>

*Funds are defined as cash, short term investments and deposits less bank overdrafts.

MacMILLAN BLOEDEL LIMITED

Consolidated Statements of Retained Earnings

	Year ended December 31		
	1989	1988	1987
	(\$ millions)		
Balance at beginning of year	\$ 874.6	\$654.7	\$482.1
Net earnings	246.7	329.8	280.6
	<u>1,121.3</u>	<u>984.5</u>	<u>762.7</u>
Deduct:			
Cash dividends:			
Preferred shares	15.6	16.9	24.4
Common shares 1989 \$.80 per share			
(1988 \$.90 and 1987 \$.82 per share)	82.1	92.4	82.8
	<u>97.7</u>	<u>109.3</u>	<u>107.2</u>
Costs of issue and redemption of class B preferred shares .....	.3	.6	.8
	<u>98.0</u>	<u>109.9</u>	<u>108.0</u>
Balance at end of year	<u>\$1,023.3</u>	<u>\$874.6</u>	<u>\$654.7</u>

AUDITORS' REPORT

To the Shareholders of
MacMillan Bloedel Limited:

We have examined the consolidated statements of financial position of MacMillan Bloedel Limited as at December 31, 1989 and 1988 and the consolidated statements of earnings, retained earnings and changes in financial position for each of the years ended December 31, 1989, 1988 and 1987. Our examinations were 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, 1989 and 1988 and the results of its operations and the changes in its financial position for the years ended December 31, 1989, 1988 and 1987 in accordance with generally accepted accounting principles consistently applied.

Price Waterhouse
Chartered Accountants

Vancouver, British Columbia
February 8, 1990

MacMILLAN BLOEDEL LIMITED

Notes to Consolidated Financial Statements December 31, 1989, 1988 and 1987

In these notes "MacMillan Bloedel" means MacMillan Bloedel Limited and its consolidated subsidiaries, and "Company" means MacMillan Bloedel Limited as a corporation.

1. Accounting policies:

MacMillan Bloedel follows accounting principles generally accepted in Canada. Information with respect to generally accepted accounting principles in the United States is provided in Note 15.

(a) Principles of consolidation

The consolidated financial statements include all subsidiaries.

(b) Foreign currency translations

The assets and liabilities of self-sustaining foreign operations are translated at current rates of exchange while those of integrated foreign operations are translated at current rates for items measured at current prices, and at historical rates for items measured at past prices. Other assets and liabilities denominated in foreign currencies are translated at the year-end rate of exchange.

MacMillan Bloedel considers that its foreign currency denominated debt represents an effective hedge of its foreign currency investments in subsidiary and partly-owned companies. Accordingly, foreign currency translation adjustments relating to long term debt are included with the foreign exchange translation adjustment relating to self-sustaining foreign operations as a separate component of shareholders' equity.

The foreign exchange translation adjustments which are separately identified in the consolidated financial statements represent the amounts required to adjust the Canadian dollar equivalents from those that are derived from using historical rates of exchange to those that are derived from using the above noted policy.

(c) Valuation of inventories

Inventories of operating and maintenance supplies and raw materials are valued at the lower of average cost and replacement cost. Inventories of manufactured products are valued at the lower of average cost and net realizable value.

(d) Property, plant and equipment

Property, plant and equipment are recorded at cost.

MacMillan Bloedel employs the units-of-production basis for depreciation of manufacturing assets. Non-manufacturing assets are depreciated on a straight-line basis.

The rates of depreciation being applied are intended to fully depreciate manufacturing assets (at normal production levels) and non-manufacturing assets over the following periods:

Buildings	20 and 40 years
Pulp and paper mill machinery and equipment	20 years
Logging machinery and equipment	5 to 7 years
Other manufacturing machinery and equipment	7 to 13 years
Vessels	10 to 13 years

Depletion of timber and amortization of main logging roads are determined on a basis related to log production.

(e) Capitalized interest

Interest is capitalized on major capital projects during construction.

(f) Goodwill

Goodwill in investments in partly-owned companies is amortized over 20 years.

2. Inventories:

	December 31	
	1989	1988
	(\$ millions)	
Operating and maintenance supplies	\$ 72.9	\$ 70.2
Logs, pulp chips and pulpwood	176.6	153.5
Lumber, panelboards and other building materials	197.6	195.3
Pulp and paper products	45.2	45.0
Containerboard and packaging products	33.8	35.7
	<u>\$526.1</u>	<u>\$499.7</u>

3. Investments accounted for by the equity method:

	December 31				
	1989		1988		
	% Owned	Cost	Undistributed earnings (losses) (\$ millions)	Total	Total
Koninklijke Nederlandse Papierfabrieken N.V. (KNP)	28.2	\$ 98.0	\$138.2	\$236.2	\$155.8
MacMillan Smurfit SCA Limited	50.0	31.6	(4.2)	27.4	22.8
MacMillan Bathurst Inc.	50.0	24.6	11.5	36.1	35.1
Island Paper Mills (partnership)	50.0	51.9	(.9)	51.0	38.7
Other		4.1	(2.9)	1.2	2.5
		210.2	141.7	351.9	254.9
Foreign exchange translation adjustment		(8.1)	36.6	28.5	21.5
		<u>\$202.1</u>	<u>\$178.3</u>	<u>\$380.4</u>	<u>\$276.4</u>

Summarized financial information —

	December 31			
	KNP	Other	Total	Total
	(\$ millions)			
Current assets	\$ 622.4	\$ 192.0	\$ 814.4	\$ 716.8
Investments accounted for by the equity method*	457.3	—	457.3	101.6
Other non-current assets	808.8	280.5	1,089.3	969.0
Foreign exchange translation adjustment	74.2	(7.6)	66.6	36.7
	<u>\$1,962.7</u>	<u>\$ 464.9</u>	<u>\$2,427.6</u>	<u>\$1,824.1</u>
Current liabilities	\$ 350.5	\$ 121.2	\$ 471.7	\$ 358.4
Non-current liabilities	696.9	125.4	822.3	618.7
Foreign exchange translation adjustment	76.6	(1.4)	75.2	62.2
	1,124.0	245.2	1,369.2	1,039.3
Shareholders' equity	708.2	230.2	938.4	691.3
Foreign exchange translation adjustment	130.5	(10.5)	120.0	93.5
	<u>\$1,962.7</u>	<u>\$ 464.9</u>	<u>\$2,427.6</u>	<u>\$1,824.1</u>

	Year ended December 31				
	1989			1988	1987
	KNP	Other	Total (\$ millions)	Total	Total
Net sales	\$1,491.1	\$ 903.3	\$2,394.4	\$2,515.2	\$2,374.0
Gross profit	\$ 188.8	\$ 31.2	\$ 220.0	\$ 267.9	\$ 209.8
Net earnings	\$ 161.8	\$ 11.0	\$ 172.8	\$ 176.1	\$ 117.3

*On January 3, 1989 KNP acquired an interest of approximately 50% in the major Austrian fine paper company Leykam-Mürztaler. On that same date MacMillan Bloedel subscribed and paid for an additional 5% common share interest in KNP. KNP also issued another 5% common share interest to the previous owners of Leykam-Mürztaler as part of the acquisition. MacMillan Bloedel paid \$46.7 million for the treasury shares and thereby increased its shareholding by 1.9%. On that same date KNP also acquired a 50% interest in Hch Sieger GmbH & Co. KG. The total goodwill resulting from these transactions amounts to approximately \$158 million.

4. Buildings and equipment

Property, plant and equipment:

	Cost	Accumulated depreciation	Net	Construction in Progress
	(\$ millions)			
December 31, 1989				
Building materials	\$ 721.1	\$ 330.3	\$ 390.8	\$ 77.2
Pulp and paper	1,352.7	615.8	736.9	46.3
Containerboard and packaging	562.4	218.5	343.9	17.4
Corporate assets and other	108.2	38.2	70.0	—
	<u>\$2,744.4</u>	<u>\$1,202.8</u>	<u>\$1,541.6</u>	<u>\$ 140.9</u>
December 31, 1988				
Building materials	\$ 578.6	\$ 320.1	\$ 258.5	\$ 50.6
Pulp and paper	1,169.2	581.3	587.9	45.4
Containerboard and packaging	526.6	200.3	326.3	—
Corporate assets and other	92.8	32.2	60.6	7.7
	<u>\$2,367.2</u>	<u>\$1,133.9</u>	<u>\$1,233.3</u>	<u>\$ 103.7</u>

Assets having an aggregate historical cost of \$184.6 million (1988 — \$188.3 million) (mainly the Alabama facilities and certain ships) and the related depreciation and long term debt included in these financial statements are held under capital leases.

The following major projects comprised MacMillan Bloedel's construction in progress as at December 31, 1989:

Parallam® plant at Colbert, Georgia, pollution projects at Harmac and Powell River, paper machine modernizations at Port Alberni, Powell River and Pine Hill and a parallel strand lumber manufacturing plant at Deerwood, Minnesota.

The estimated total cost of these projects, including capitalized interest, is \$474.0 million. These projects will be completed in 1990 and 1991.

5. Short term bank indebtedness:

At December 31, 1989 MacMillan Bloedel had short term bank lines of credit aggregating \$287.8 million (1988 — \$264.7 million) of which \$37.0 million (1988 — \$42.7 million) had been drawn down.

6. Payments on long term debt and retractable preferred shares in the next five years:

	Bonds	Term bank loans	Other liabilities	Subtotal	Retractable preferred shares	Total
	(\$ millions)					
1990 .....	.7	14.4	3.7	18.8	2.2	21.0
1991 .....	.7	22.3	4.9	27.9	2.2	30.1
1992 .....	.7	4.6	3.6	8.9	19.2	28.1
1993	4.4	2.4	4.1	10.9	—	10.9
1994 .....	.8	89.3	4.4	94.5	—	94.5

7. Term loans (unsecured):

	December 31	
	1989	1988
	(\$ millions)	
9.2% U.S.\$200.0 million maturing December 14, 1999.....	\$232.7	\$ —
8.1% Dutch Guilders 215.0 million maturing October 16, 1996	118.0	—
8.31% U.S. \$50.0 million maturing March 28, 1994	65.4	65.4
8.54% U.S. \$25.0 million maturing April 1, 1994	32.6	32.6
7.39% Dutch Guilders 53.4 million maturing September 15, 1991	27.1	33.6
5.34% Yen 1,300 million maturing September 30, 1993	11.8	9.2
5.1% Yen 200 million maturing March 31, 1992	1.7	—
6.5% Yen 200 million maturing December 31, 1992	1.7	—
Advances under contractual term lines of credit	—	34.8
	491.0	175.6
Less: Payments due within one year	12.3	6.5
	<u>\$478.7</u>	<u>\$169.1</u>

At December 31, 1989 MacMillan Bloedel had contractual term bank lines of credit aggregating \$650.0 million (1988 — \$650.0 million) of which \$NIL million (1988 — \$34.8 million) had been drawn down. These contractual term lines provide for loans on a revolving basis for up to three years, followed by repayment periods of five years.

8. Notes, bonds and debentures:

	December 31	
	1989	1988
	(\$ millions)	
MacMillan Bloedel Limited — (unsecured)		
9% Notes maturing March 5, 1996		
(U.S. \$100.0 million)	\$133.3	\$133.3
MacMillan Bloedel Inc.* —		
10¼% to 10½% industrial development revenue and pollution control bonds,		
maturing 1993 to 2015 (U.S. \$31.4 million)	37.8	37.8
MacMillan Bloedel of America Inc.* —		
Industrial bonds at interest rates ranging from 4.90% to 10¼% and maturing from		
1993 to 1997 (U.S. \$5.2 million)	6.5	6.5
	177.6	177.6
Less: Payments due within one year .....	.8	—
	<u>\$176.8</u>	<u>\$177.6</u>

*These bonds are direct obligations of Industrial Development Boards and municipal authorities in Alabama, Arkansas and Mississippi.

9. Convertible subordinated debentures (unsecured):

On May 21, 1987 the Company issued \$150.0 million twenty year adjustable rate convertible subordinated debentures.

Interest —

The interest rate is the greater of (i) 5% and (ii) 1% plus the percentage that two times the dividends paid per common share in the previous six months is of the then applicable conversion price.

Conversion features —

The debentures are convertible at the holder's option into common shares on or before the earlier of the last business day prior to the maturity date of the debentures or the last business day prior to redemption, at a conversion price of \$28.625 per common share subject to adjustment under certain antidilution or other provisions.

Redemption features —

At the Company's option, the debentures are redeemable after May 1, 1990; upon maturity they are redeemable for common shares. The characteristics and attributes attaching to the convertible subordinated debentures, including the Company's option to require the trustee to apply the proceeds and purchase common shares, causes the Company to view these securities as substantially permanent capital and consequently these debentures are shown under the heading "convertible debentures and shareholders equity".

10. Share capital:

Common share capital reflects the subdivision of each common share into three common shares on April 9, 1987.

The Company's authorized capital consists of 250.0 million common shares, 3.4 million class A preferred shares and 20.0 million class B preferred shares issuable in series, all without par value.

	December 31	
	1989	1988
	(\$ millions)	
Outstanding shares without par value		
Preferred —		
203,129 class B, series 4	\$ 18.1	\$ 19.7
1,919,800 class B, series 8	48.0	49.5
1,000 class B, series 9	—	—
2,341,200 class B, series 10	58.5	59.4
	124.6	128.6
Foreign exchange translation adjustment	(1.1)	(.7)
	123.5	127.9
Common —		
102,649,825 shares	552.0	552.0
	<u>\$675.5</u>	<u>\$679.9</u>

The Class A Preferred Shares —

The class A preferred shares were retracted on May 1, 1987 at a cost of U.S.\$85.0 million.

The Class B Preferred Shares —

These shares rank prior to the common shares of the Company.

10. Share Capital: (continued)

	<u>Date</u>	<u>Price</u>
Redemption features		
Series 4:		
Company's redemption options — redeemable before	September 1, 1992	U.S.\$100.00
Company's redemption obligations — redeem 4,687 shares	September 1, 1987	
each quarter	through June 1, 1992	U.S.\$100.00
redeem remaining shares on	September 1, 1992	U.S.\$100.00
Series 8:		
Company's redemption options — redeemable after	September 1, 1990	\$26.00 ⁽¹⁾
Company's redemption obligations — make all reasonable		
efforts to purchase, during each calendar quarter		
(i) ½% of the shares outstanding	March 1, 1987	\$25.00
on February 28, 1987 and	to September 1, 1990	maximum
(ii) 1% of the shares outstanding		\$25.00
on August 31, 1990	September 1, 1990	maximum
Series 10:		
Company's redemption options — redeemable on or after	March 1, 1991	\$25.50 ⁽²⁾
Company's redemption obligations — make all reasonable		
efforts to purchase, during each calendar quarter, ½% of	September 1, 1987	\$25.00
the shares outstanding on August 31, 1987	to February 28, 1991	maximum

(1) This price declines \$.50 annually to \$25.00.

(2) This price reduces to \$25.00 on or after March 1, 1993.

Dividends

- Series 4 Cumulative preferential equal to the sum of 1½% and ½ of the defined average U.S. prime rate per annum, payable quarterly.
- Series 8 Cumulative preferential of 9¼% to September 1, 1990 and 73% of the Canadian prime interest rate thereafter.
- Series 9 Dividends are payable only to the extent of revenues received by the Company from certain oil and gas property interests. The holder of the series 9 preferred shares is also entitled to participate in dividends distributed to common shareholders.
- Series 10 Cumulative preferential; until March 1, 1991 of \$2.175 per share (8.7%) per annum payable quarterly (thereafter, payable monthly). Commencing March 1, 1991 the dividend rate is related to changes in prime. The initial annual floating dividend rate equals 73% of prime.

Share purchase plans —

Employee

The Company has reserved 7.5 million common shares for issuance pursuant to the employee share purchase plan of which 6.3 million had been taken up as at December 31, 1989.

Senior management

At December 31, 1989 loans to employees under the senior management share purchase plan amounted to \$9.1 million (1988 — \$5.8 million). The loans are non-recourse, interest free, maturing June 25, 1991, June 1, 1997, June 1, 1998 or April 1, 1999 and secured by a pledge of the common shares.

Options to purchase common shares

Options for 36,152 shares were exercised and options for 17,683 shares were relinquished during 1987. There were no outstanding options at December 31, 1988 and 1989.

Convertible subordinated debentures

The Company has reserved 5.2 million common shares for issuance pursuant to the terms of issue of the convertible subordinated debentures.

Changes in share capital —

	Issued and Outstanding	
	Number of shares	(\$ millions)
Class A preferred shares		
January 1, 1987	3,400,000	\$ 87.9
Retracted during 1987	(3,400,000)	(87.9)
December 31, 1989	<u>—</u>	<u>\$ —</u>
Class B preferred shares		
Series 1		
January 1, 1987	1,735,802	\$ 43.4
Converted to 4,040,130 common shares during 1987	(1,718,152)	(43.0)
Pro-forma balance December 31, 1986	17,650	.4
Redeemed during 1987	(5,856)	(.1)
Converted to 27,672 common shares during 1987	(11,794)	(.3)
December 31, 1989	<u>—</u>	<u>\$ —</u>
Series 2		
January 1, 1987	1,986,468	\$ 49.7
Redeemed during 1987	(6,912)	(.2)
Converted to 3,845,283 common shares during 1987	(1,979,556)	(49.5)
December 31, 1989	<u>—</u>	<u>\$ —</u>
Series 3		
January 1, 1987	227,250	\$ 22.7
Redeemed during 1987	(227,250)	(22.7)
December 31, 1989	<u>—</u>	<u>\$ —</u>
Series 4		
January 1, 1987	250,000	\$ 22.3
Redeemed during 1987	(9,375)	(.9)
December 31, 1987	240,625	21.4
Redeemed during 1988	(18,748)	(1.7)
December 31, 1988	221,877	19.7
Redeemed during 1989	(18,748)	(1.6)
December 31, 1989	<u>203,129</u>	<u>\$ 18.1</u>
Series 6		
January 1, 1987	2,000,000	\$ 50.0
Purchased during 1987	(6,800)	(.2)
December 31, 1987	1,993,200	49.8
Purchased during 1988	(1,993,200)	(49.8)
December 31, 1989	<u>—</u>	<u>\$ —</u>
Series 8		
January 1, 1987	2,000,000	\$ 50.0
Purchased during 1987	(11,100)	(.3)
December 31, 1987	1,988,900	49.7
Purchased during 1988	(9,100)	(.2)
December 31, 1988	1,979,800	49.5
Purchased during 1989	(60,000)	(1.5)
December 31, 1989	<u>1,919,800</u>	<u>\$ 48.0</u>

10. Share Capital: (continued)

Changes in share capital — (continued)

	Issued and Outstanding	
	Number of shares	(\$ millions)
Series 9		
Issued in 1985		
December 31, 1989	1,000	\$ —
Series 10		
January 1, 1987	2,400,000	\$ 60.0
Purchased during 1987	(13,900)	(.3)
December 31, 1987	2,386,100	59.7
Purchased during 1988	(10,100)	(.3)
December 31, 1988	2,376,000	59.4
Purchased during 1989	(34,800)	(.9)
December 31, 1989	2,341,200	\$ 58.5
Common shares		
January 1, 1987	93,794,763	\$438.2
Conversion of class B preferred shares during January 1987	4,040,130	43.0
Pro-forma balance, December 31, 1986	97,834,893	481.2
Conversion of class B preferred shares	3,872,955	49.8
Employee share purchase plan	703,358	16.4
Share options	36,152	.2
December 31, 1987	102,447,358	547.6
Employee share purchase plan	202,467	4.4
December 31, 1988 and December 31, 1989	102,649,825	\$552.0

11. Commitments:

In addition to commitments for capital expenditures and the future supply of operating services and materials, MacMillan Bloedel is committed at December 31, 1989 in respect of the following —

- (a) Ship charters and rentals under non-cancellable operating leases having an initial term of more than one year as follows —

	Ship charters	Leases (\$ millions)	Total
1990	\$24.0	\$16.0	\$ 40.0
1991	24.3	11.6	35.9
1992	19.8	5.3	25.1
1993	6.6	4.3	10.9
1994	—	3.7	3.7
1995 - 1999	—	7.3	7.3
2000 - 2004	—	4.2	4.2
2005 - 2009	—	.8	.8
	<u>\$74.7</u>	<u>\$53.2</u>	<u>\$127.9</u>

- (b) The acquisition of timber in Alabama under long term cutting contracts requiring minimum annual payments (extending in some cases to the year 2034); payment of approximately \$5.4 million is required in each of the next five years.

12. Earnings statements supplementary information:

(a) *Costs and expenses*

	Year ended December 31		
	1989	1988	1987
	(\$ millions)		
Interest expense			
Long term debt interest	\$ 34.2	\$ 35.0	\$ 43.5
Convertible debenture interest	7.6	7.5	4.6
Other interest	26.0	5.0	5.6
	67.8	47.5	53.7
Less: Interest capitalized	14.2	4.0	3.0
	<u>\$ 53.6</u>	<u>\$ 43.5</u>	<u>\$ 50.7</u>
Effective average interest rate	<u>8%</u>	<u>8%</u>	<u>8%</u>
Other income (expense)			
Income from investments	\$ 4.3	\$ 4.3	\$ 6.7
Other	7.2	(13.4)	11.1
	<u>\$ 11.5</u>	<u>\$ (9.1)</u>	<u>\$ 17.8</u>
Depreciation	\$109.8	\$106.4	\$ 106.8
Depletion	13.0	10.5	13.8
Amortization	7.6	7.7	6.8
	<u>\$130.4</u>	<u>\$124.6</u>	<u>\$ 127.4</u>
Research and development expenses	\$ 16.1	\$ 15.2	\$ 15.1
Less: Government grants and investment tax credits	3.6	3.9	4.6
	<u>\$ 12.5</u>	<u>\$ 11.3</u>	<u>\$ 10.5</u>
Rental expense	\$ 49.7	\$ 52.3	\$ 52.0
Remuneration of directors and executive officers	\$ 6.9	\$ 6.2	\$ 6.2
Wages, salaries and benefits	\$773.3	\$739.3	\$ 708.2
Pension expense (Note 14)	<u>\$ 60.7</u>	<u>\$ 55.5</u>	<u>\$ 45.9</u>

(b) *Income taxes*

Consolidated income tax expense:

Years ended December 31	Canadian federal	Canadian provincial	Foreign	Total
		(\$ millions) expense (recovery)		
1989				
Current	\$30.4	\$19.7	\$40.3	\$ 90.4
Deferred	17.6	12.0	3.5	33.1
	<u>\$48.0</u>	<u>\$31.7</u>	<u>\$43.8</u>	<u>\$123.5</u>
1988				
Current	\$54.9	\$38.1	\$40.3	\$133.3
Deferred	17.7	12.0	(1.6)	28.1
	<u>\$72.6</u>	<u>\$50.1</u>	<u>\$38.7</u>	<u>\$161.4</u>
1987				
Current	\$ 9.8	\$ 4.4	\$33.1	\$ 47.3
Deferred	75.0	48.7	12.8	136.5
	<u>\$84.8</u>	<u>\$53.1</u>	<u>\$45.9</u>	<u>\$183.8</u>

12. Earnings statements supplementary information: (continued)

(b) *Income taxes*

Consolidated income tax expense:

The principal items giving rise to deferred income tax expense are depreciation, depletion and amortization.

Income tax rate reconciliation:

	Year ended December 31		
	1989	1988	1987
Canadian federal income tax rate	38.0%	41.5%	45.5%
Provincial and state taxes and federal surtax	4.0	3.5	4.1
Canadian manufacturing and processing allowance	(1.2)	(2.5)	(3.6)
Foreign tax rates	(3.3)	(2.3)	(2.1)
Other items .....	.7	(3.1)	(1.5)
Effective income tax rate	<u>38.2%</u>	<u>37.1%</u>	<u>42.4%</u>

(c) *Net earnings per common share*

Basic net earnings per common share is computed by dividing the net earnings, after providing for dividends on the preferred shares, by the weighted average number of shares outstanding during the year. The provision for dividends on the preferred shares is made on a time elapsed basis rather than on a declared basis.

Fully diluted net earnings per common share is computed by dividing basic net earnings (adjusted for the after tax interest expense on the convertible subordinated debentures) by the weighted average number of shares outstanding during the period (adjusted for the number of common shares which would have been issued had the conversion taken place at the beginning of the year).

13. Related party transactions:

MacMillan Bloedel sells products and services in the ordinary course of business and at fair market values to related parties and also purchases certain services and products for resale from related parties. These transactions include the sale of pulp to Koninklijke Nederlandse Papierfabrieken N.V., and Island Paper Mills Company, the sale of containerboard to MacMillan Bathurst Inc. and MacMillan Smurfit SCA Limited and the purchase of lumber from Noranda Forest Inc.

	Year ended December 31		
	1989	1988	1987
	(\$ millions)		
Sales to related parties	<u>\$115.4</u>	<u>\$109.1</u>	<u>\$101.5</u>
Purchases from related parties	<u>\$ 73.8</u>	<u>\$ 81.7</u>	<u>\$ 61.1</u>
	December 31		
	1989	1988	
	(\$ millions)		
Accounts receivable from related parties	<u>\$ 18.0</u>	<u>\$ 18.9</u>	

In addition to the items in the ordinary course of business in 1987, MacMillan Bloedel sold its Brazilian investment to Brascan Limited for \$10.9 million, purchased 100,000 KNP shares from Noranda Forest Inc. for \$7.6 million and sold \$90.0 million adjustable rate convertible subordinated debentures series 1 for \$87.5 million to Great Lakes Group Inc.

14. Pension plans:

Substantially all employees may participate in pension plans after one or two years service. All the salaried employees are members of company sponsored plans. Salaried pension plan amendments to increase payments to pensioners and increase pensions for present employees were approved during 1988. The \$23.5 million cost of these amendments is being amortized to earnings over appropriate periods. The hourly employees are generally

members of negotiated plans to which the Company contributes amounts specified by collective agreements. In addition, the Company has agreements with some of its officers and executives (including retirees) which call for payments to be made under certain conditions following retirement.

Consolidated summary of Company sponsored pension plans:

	December 31		
	1989	1988	1987
	(\$ millions)		
Pension fund assets at market related values	\$398.8	\$363.4	\$368.3
Obligations for pension benefits	<u>454.6</u>	<u>418.6</u>	<u>385.7</u>
Excess of obligations over fund assets	55.8	55.2	17.4
Provisions	<u>24.1</u>	<u>24.4</u>	<u>6.1</u>
Excess of obligations over provision and fund assets	<u>\$ 31.7</u>	<u>\$ 30.8</u>	<u>\$ 11.3</u>

15. Information with respect to United States generally accepted accounting principles (U.S. GAAP):

There are no material differences between MacMillan Bloedel's consolidated net earnings determined in accordance with U.S. GAAP and consolidated net earnings determined in accordance with generally accepted accounting principles in Canada.

The balance sheet captions listed below are specifically shown for compliance with requirements of the United States Securities and Exchange Commission (SEC):

	December 31	
	1989	1988*
	(\$ millions)	
Total assets	\$3,258.1	\$2,753.1
Current assets	967.3	932.0
Current liabilities	486.8	454.3

*Certain 1988 amounts have been reclassified to conform with the presentation in 1989.

The SEC requires that redeemable preferred shares not be shown as part of shareholders' equity. Accordingly, under SEC requirements shareholders' equity would be:

	December 31	
	1989	1988
	(\$ millions)	
Common shares	\$ 552.0	\$ 552.0
Retained earnings — U.S. GAAP	<u>1,023.3</u>	<u>874.6</u>
	1,575.3	1,426.6
Foreign exchange translation adjustment	<u>(66.3)</u>	<u>(50.2)</u>
	<u>\$1,509.0</u>	<u>\$1,376.4</u>

16. Segment information:

	Sales from Canada to	Sales to unaffiliated customers from	Contributions to operating earnings (2)	Assets*
		(\$ millions)		
Year ended December 31, 1989				
Canada	\$ 609.4	\$1,468.6	\$313.2	\$1,764.4
United States	836.1	1,523.8	110.9	905.7
Europe	348.9	42.4	1.0	12.2
Japan and other	647.6	238.9	15.6	81.4
	2,442.0	3,273.7	440.7	2,763.7
Eliminations and adjustments:				
Inter-segment			(4.9)	(20.2)
General corporate			(59.2)	549.2
Foreign exchange translation adjustment				(34.6)
Interest expense			(53.6)	
Consolidated totals	<u>\$2,442.0</u>	<u>\$3,273.7</u>	<u>\$323.0</u>	<u>\$3,258.1</u>
Year ended December 31, 1988				
Canada	\$ 566.7	\$1,440.8	\$422.7	\$1,503.4
United States	932.0	1,595.7	128.2	778.5
Europe	336.5	51.5	(.3)	18.0
Japan and other	632.9	185.5	3.7	74.9
	2,468.1	3,273.5	554.3	2,374.8
Eliminations and adjustments:				
Inter-segment			9.3	(15.3)
General corporate			(84.7)	381.2
Foreign exchange translation adjustment				12.4
Interest expense			(43.5)	
Consolidated totals	<u>\$2,468.1</u>	<u>\$3,273.5</u>	<u>\$435.4</u>	<u>\$2,753.1</u>
Year ended December 31, 1987				
Canada	\$ 559.3	\$1,343.2	\$412.3	\$1,307.2
United States	951.2	1,566.5	115.0	722.5
Europe	294.9	83.4	.2	22.3
Japan and other	547.1	141.4	11.2	41.7
	2,352.5	3,134.5	538.7	2,093.7
Eliminations and adjustments:				
Inter-segment			(9.3)	(24.6)
General corporate			(45.8)	363.6
Foreign exchange translation adjustment				83.1
Interest expense			(50.7)	
Consolidated totals	<u>\$2,352.5</u>	<u>\$3,134.5</u>	<u>\$432.9</u>	<u>\$2,515.8</u>

*Prior years have been reclassified to conform with the presentation in 1989.

	Total revenue	Contributions to earnings (1) (2)	Depreciation, depletion and amortization (\$ millions)	Capital expenditures	Assets*
Year ended December 31, 1989					
Building materials	\$1,408.6	\$139.1	\$ 57.0	\$246.8	\$1,161.3
Pulp and paper	1,310.2	180.8	42.1	194.5	1,081.1
Containerboard and packaging	504.1	113.6	21.7	59.4	473.1
Other	50.8	2.3	1.8	.1	28.0
Total operations	3,273.7	435.8	122.6	500.8	2,743.5
General corporate		(59.2)	7.3	17.6	549.2
Foreign exchange translation adjustment .....			.5		(34.6)
Interest expense		(53.6)			
Consolidated totals	<u>\$3,273.7</u>	<u>\$323.0</u>	<u>\$130.4</u>	<u>\$518.4</u>	<u>\$3,258.1</u>
Year ended December 31, 1988					
Building materials	\$1,404.7	\$186.8	\$ 58.8	\$170.0	\$ 960.9
Pulp and paper	1,282.5	254.9	36.6	146.5	922.7
Containerboard and packaging	530.1	118.0	23.9	32.8	443.8
Other	56.2	3.9	2.6	.3	32.1
Total operations	3,273.5	563.6	121.9	349.6	2,359.5
General corporate		(84.7)	1.0	14.4	381.2
Foreign exchange translation adjustment			1.7		12.4
Interest expense		(43.5)			
Consolidated totals	<u>\$3,273.5</u>	<u>\$435.4</u>	<u>\$124.6</u>	<u>\$364.0</u>	<u>\$2,753.1</u>
Year ended December 31, 1987					
Building materials	\$1,429.8	\$206.4	\$ 57.0	\$ 73.5	\$ 827.7
Pulp and paper	1,145.3	229.6	33.7	122.6	779.6
Containerboard and packaging	506.1	88.9	23.6	19.5	429.4
Other	53.3	4.5	3.0	27.1	32.4
Total operations	3,134.5	529.4	117.3	242.7	2,069.1
General corporate		(45.8)	5.7	13.9	363.6
Foreign exchange translation adjustment			4.4		83.1
Interest expense		(50.7)			
Consolidated totals	<u>\$3,134.5</u>	<u>\$432.9</u>	<u>\$127.4</u>	<u>\$256.6</u>	<u>\$2,515.8</u>

*Prior years have been reclassified to conform with the presentation in 1989.

(1) *Basis of segmentation*

MacMillan Bloedel carries on an integrated forest products business which involves extensive transfers of raw materials and products among operations. Segmenting an integrated forest products business into product and service categories involves allocating conversion and other costs and raw material costs. Raw material costs are allocated on a basis proportionate to the end product net revenue before deducting fibre cost. Other pricing policies and methods of allocating costs are possible but at this time the Company believes the above determined method to be appropriate to its circumstances.

(2) *Contributions to operating earnings*

Contributions to operating earnings represent sales of products and services less cost of sales and services, selling expenses and allocated general and administrative expenses.

16. Segment information: (continued)

(2) Contributions to operating earnings (continued)

General corporate profit and loss items consist of unallocated corporate staff expenses, profit and loss on asset disposals, corporate research, foreign exchange and one time items not attributed to a line of business. General corporate items in assets are mainly short term investments, investments and other assets and certain fixed assets such as computers and research facilities.

(3) Sales of products and services

Treated poles, pilings and export log sales are included in building material sales.

17. Subsidiary companies and jurisdiction of incorporation: (100% owned unless otherwise noted)

British Columbia

Altair Property and Casualty Corporation
Canadian Transport Company (International)
Limited
Canadian Transport Company Limited
Forest Industries Flying Tankers Limited
(57.5% interest)
Island Paper Mills Limited*
Kingcome Navigation Company Ltd.
MacMillan Bloedel Building Limited*
MacMillan Bloedel Building Materials Limited
MacMillan Bloedel Parallam Services Limited*
Port Royal Development Limited
Vancouver Marine Engines Ltd.

Saskatchewan

MacMillan Bloedel (Saskatchewan) Limited*

Ontario

MacMillan Bloedel Export Sales Ltd.*
MacMillan Bloedel (Thunder Bay) Limited*

Alabama

MacMillan Bloedel of America Inc.
MacMillan Bloedel Inc.
MacMillan Bloedel Financial Inc.
MacMillan Bloedel Holdings Inc.*
MacMillan Bloedel Particleboard Inc.
MacMillan Bloedel Radio System, Inc.*
MacMillan Bloedel Timberlands Inc.

Delaware

Powell River-Alberni Sales Corporation
MacMillan Bloedel (USA) Inc.

Washington

Fibres International, Inc. (51% interest)

*Inactive

Australia

Canadian Transport Company Pty. Limited*
MacMillan Bloedel Pty. Limited

Barbados

Canadian Transport Company (Overseas)
Limited*
Camarin Limited
MacMillan Bloedel Finance Limited
MacMillan Bloedel FSC Ltd.

England

Hygrade Corrugated Cases Limited*
MacMillan Bloedel Containers Holdings Limited*
MacMillan Bloedel Holdings (UK) Limited*
MacMillan Bloedel Pulp and Paper Sales Limited

Hong Kong

MacMillan Bloedel (Asia) Limited

Japan

MacMillan Bloedel K.K.

Malaysia

MacMillan Bloedel (South East Asia) SDN.BHD.

Netherlands

MacMillan Bloedel Europe B.V.
MacMillan Bloedel (Limburg) N.V.

Netherlands Antilles

Canadian Maas River Investment N.V.
MacMillan Bloedel (Curacao) N.V.*
MacMillan Bloedel St. Maarten N.V.

