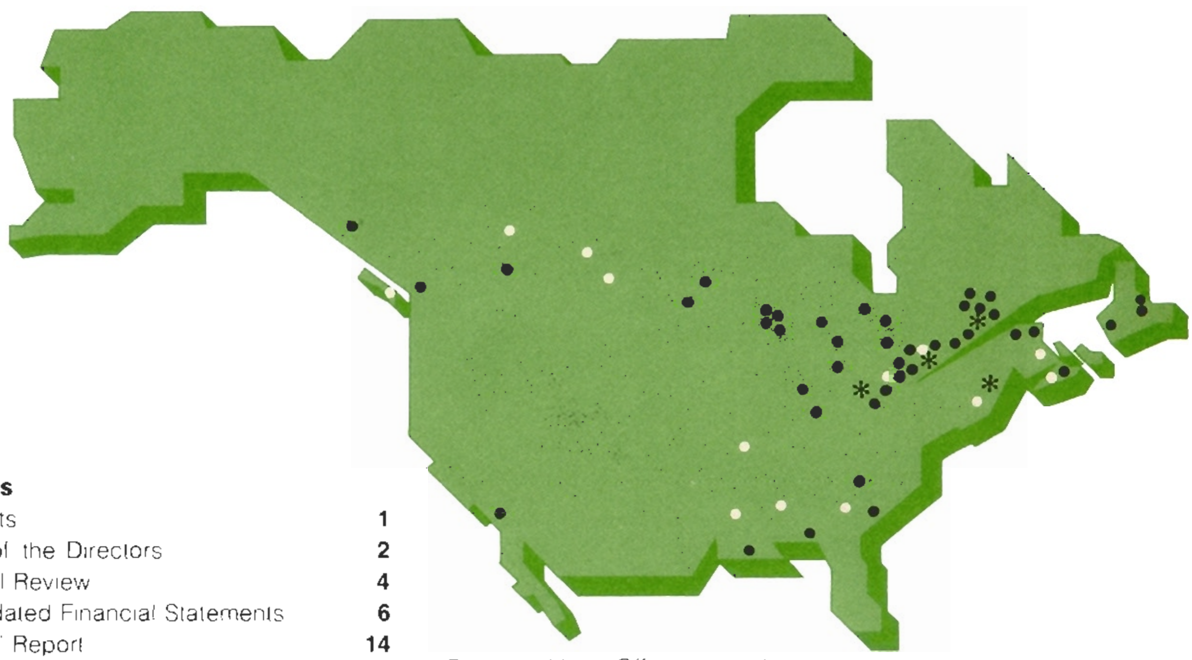
ABITIBI Annual Report for the year ended December 31, 1978



Principal Head Offices *
Mills/Plants •
Marketing/Sales Offices

Contents

Abitibi Paper Company Ltd.
Head Office Toronto-Dominion Centre,
Toronto, Canada M5K 1B3

The Annual Meeting
To be held in Commerce Hall, Concourse Level, Commerce Court West, Toronto Canada on Monday, April 23, 1979 at 10:30 a.m. Toronto time
We encourage you to attend. If you are not able to, we ask you to sign your proxy and return it to the Registrar

On peut obtenir ce rapport annuel en francais sur demande

Abitibi is . . .

A natural resource based company. Abitibi is a major employer numbering more than 18,000 people in Canada and nearly 2,000 in the United States

A Canadian-owned company, Abitibi is the world's largest manufacturer of newsprint. In total, the company manufactures over three million tons of paper, pulp and wood products annually, the output from 40 mills and plants in Canada and the United States as pinpointed on our map

Distribution of Common Shares

December 31, 1978

	Shareholders		Shares	
	No.	%	No.	%
Alberta	543	3.04	268,036	1.44
British Columbia	1,209	6.76	549,093	2.94
Manitoba	461	2.58	1,277,770	6.84
New Brunswick	345	1.93	84,736	0.45
Newfoundland	41	0.23	15,112	0.08
Nova Scotia	522	2.92	202,839	1.09
Ontario	9,534	53.32	11,484,473	61.52
Prince Edward Island	44	0.25	7,543	0.04
Quebec	3,661	20.47	3,577,034	19.16
Saskatchewan	204	1.14	51,665	0.28
Other Canadian	5	0.03	270	–
Total Canadian	16,569	92.67	17,518,571	93.84
U.S.A.	1,115	6.24	985,487	5.28
Foreign	195	1.09	164,186	0.88
Total	17,879	100.00	18,668,244	100.00

Highlights

(thousands of dollars except per share calculations)	1978	1977	% Change
Sales, less delivery expenses	$1 295 699	$1 043 059	24.2
Depreciation and depletion	$ 48 307	$ 43 963	9.9
Income taxes	$ 63 738	$ 29 363	117.1
Mining income	$ 2.478	$ 3.283	(24.5)
Earnings before extraordinary items	$ 78 650	$ 37.908	107.5
Per common share	$ 3.98	$ 1.83	117.5
Net earnings	$ 78 345	$ 36.221	116.3
Per common share	$ 3.96	$ 1.74	127.6
Dividends declared – preferred shares	$ 4.703	$ 4 366	7.7
– common shares	$ 17 680	$ 6 446	174.3
– per common share	$ .95	$ .35	171.4
Additions to fixed assets	$ 59 163	$ 43 580	35.8
Working capital	$ 300,673	$ 259,836	15.7
Long-term debt	$ 241,165	$ 242.512	(0.6)
Book value of common shares	$ 348 388	$ 292 424	19.1
Per common share	$ 18.66	$ 15.77	18.3

Common share market information

1978	High	Low	Close	Shares Outstanding (000's)	Shares Traded (000's)	Dividends Paid
First quarter	$12 3/8	$10 1/8	$12 3/8	18 547	885	$0.15
Second quarter	13 1/4	12 1/8	12 7/8	18.550	1 057	0.15
Third quarter	19 1/8	12 5/8	18 1/8	18 619	3 366	0.15
Fourth quarter	20 1/4	15 3/4	19 3/4	18 668	3 581	0.25
Year	20 1/4	10 1/8	19 3/4	18 668	8.889	0.70
1977	11 1/2	8 3/4	10 7/8	18 547	2.192	0.20

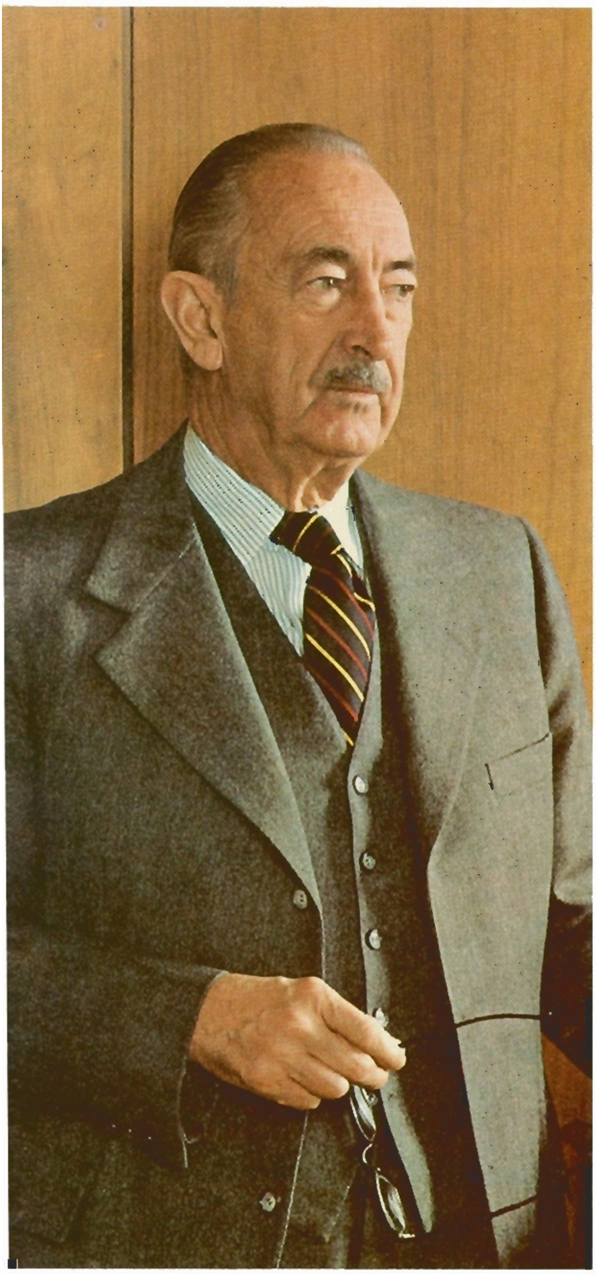
Common shares and options on common shares are listed for trading on the Toronto, Montreal and Vancouver Stock Exchanges.

Valuation Day (Dec. 22, 1971) share prices	
Common	$ 7.25
7 1/2% Cumulative Redeemable Preferred Series A	$49.50

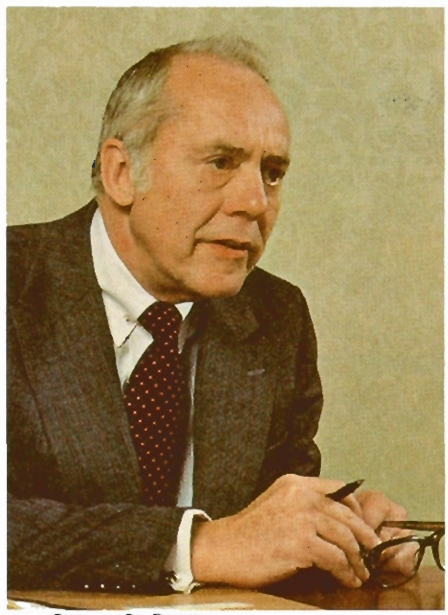
Dividend Policy

It is your Company's intention to pay out as common share dividends an average of 30-40% of the earnings available to common shareholders.

ABITIBI Report of the Directors



Thomas J. Bell
Chairman of the Board and Chief Executive Officer



Robert C. Gimlin
President and Chief Operating Officer

C. Harry Rosier
Vice-Chairman of the Board

Our consolidated net sales reached another new record of $1 295.7 million, a 24% gain over 1977.

Net earnings for the year were $78.3 million, a marked improvement over prior years and reflected a return on sales of 7.3% and on capital employed of 13.0%.

The most significant factors that affected the operating results of your Company in the year just ended were:

1. using par as the base, the premium on the U.S. dollar accounted for $41.4 million or 52.8% of our 1978 earnings as compared with $16.6 million or 45.8% in 1977. Eliminating this exchange benefit from our 1978 earnings would reduce the return on our sales dollar and on our capital employed to 3.6% and 6.9% respectively;
2. strong demand for newsprint led to a close-to-capacity operation in our mills throughout the year by comparison with an average operating rate in 1977 of about 85%;
3. there was a major turn-around in our fine paper manufacturing operations reflecting unusually good demand for these grades in the Canadian market which coincided with a substantial reduction in U.S. imports brought about, in part, by the weakness in the Canadian dollar. In addition, in 1978, we corrected the severe operating problems that we had experienced earlier at our Provincial Port Arthur mill;
4. our lumber group, which had operated at a loss in 1977, made an important contribution to our 1978 earnings;
5. earnings improved in each of the business units within our fine paper converting and distribution group. This, in combination with the divestiture of some unprofitable operations of Price Wilson, led to a satisfactory increase in the earnings of this group over 1977.

There were a number of other events in 1978 that will influence the future of your Company.

In early fall, following negotiations that had been under way for several months, we took the initial step to acquire the balance of the outstanding shares of The Price Company Limited. By year end, Abitibi owned nearly all of the common shares of Price and proceedings are under way to acquire the balance. We expect that our additional investment in Price, after financing costs, should add about 45¢ a share to our 1979 earnings.

It is our intention that Price will continue to maintain its head office in Quebec City and have its own Board of Directors. Because the association of our two companies, Abitibi and Price, has turned out so successfully, we are planning at an early date to change the name of Abitibi Paper Company Ltd. to Abitibi-Price Inc. to give credit to the important role that Price plays in our future.

Another major achievement during the year was the success of our bid to purchase the

Labrador Linerboard mill at Stephenville Newfoundland. We plan to convert this mill to a newsprint operation by late 1980, with its wood partly supplied from the timber limits that also serve our Grand Falls mill. The plant is located on tidewater and our Sales company is confident that we can sell its output in the years ahead.

During the year, we successfully completed contracts with most of the unions at our primary operations and without incurring any work stoppages. This, we feel, reflects positive negotiations and is a credit to our industry and to our unions. We have all worked very hard since the prolonged strike in 1976 to improve our communications and the work environment at all locations. This is a continuing program.

Following our last annual shareholders' meeting, C.H. Rosier, your President and Chief Operating Officer, suffered a heart attack and has since been advised to reduce his work load. He is now back at work and has been appointed Vice-Chairman of the Board. As of September 1, R.C. Gimlin, Chief Executive Officer of Abitibi-Price Sales Corporation in New York, was appointed President and Chief Operating Officer.

Early in 1978 it became apparent that with our operations running at capacity and benefiting from a favourable exchange rate, we were going to have the opportunity to begin generating the funds needed to improve the productivity of our plants, resolve our environmental problems and provide new capacity and new jobs for Canadians in the pulp and paper industry. This added a new dimension to the regular updating of the Company's five-year strategic plan that was under way. Out of this work, capital programs have been developed that could involve new investment by the Abitibi-Price group of close to $700 million over the next five years. This five-year capital spending program envisions investment of $340 million for modernization and improved efficiency in our mills, $230 million for increased capacity in a number of product lines including an additional 250,000 tons per year of newsprint, and $130 million to meet environmental requirements.

To encourage capital investment, the federal government recently improved the investment tax credit program for qualified investments in Canada. Most of our Canadian manufacturing facilities are located in those areas of the country where a 10% investment tax credit is available. Capital programs to be carried out at our mills in the Gaspé and Newfoundland have an even more attractive investment tax credit rate of 20%. These more favourable tax incentives, in combination with the heavy capital expenditures we plan for 1979, are major factors contributing to a significant reduction in the effective tax rate that we anticipate in 1979.

More recently, Ontario and Quebec have announced major programs to assist our industry to modernize and overcome costly environmental problems. The federal government has also announced its intention to complement these Provincial programs. This is an encouraging thrust. We welcome the initiatives taken by these governments to assist industry efforts in overcoming some of the cost disadvantages that we face in competing in the international marketplace.

While we anticipate some slowdown in the North American economy in 1979, we are nevertheless optimistic about the outlook for Abitibi in the coming year. The Company's newsprint and uncoated groundwood paper mills are expected to operate at capacity throughout the year. The forecasts for our fine paper and building materials groups show an improvement in their contributions to net earnings. The outlook for our lumber operations is somewhat less certain although so far this year their performance has exceeded our expectations. As mentioned earlier, we are anticipating the benefit of a lower effective tax rate and a net improvement in our share of the earnings of Price. Partly offsetting these positive factors, we look for some progressive strengthening in the value of the Canadian dollar. On balance, 1979 should show an improvement in both sales and earnings over 1978.

During the last half of the year we lost two important directors of your Company. Charles Lake Gundy—the longest serving member of your Board—died in September. He had been a loyal and dedicated director since 1952. Norman J. MacMillan died in October and he also, had been an extremely helpful director since 1974. We shall miss their wise counsel but, even more, their warm and very personal friendship.

We are happy to welcome C. Edward Medland, President and Chief Executive Officer of Wood Gundy Limited, who joined your Board in early 1978 and Howard W. Blauvelt, Chairman and Chief Executive Officer of Continental Oil Company, Stamford, Connecticut, who joined your Board in December, 1978.

I would like to pay special tribute to all our loyal, faithful and hard-working members of the family who jointly contributed to a great year for Abitibi and Price.

On behalf of the Board,

T. Bell.

Chairman and Chief Executive Officer
Toronto, February 19, 1979

Financial Review

J. Ian McGibbon

The report of the Directors sets out the total dollar amount by which earnings were improved as the result of the weakness of the Canadian dollar. At current sales levels, it is estimated that each one cent change in the U.S. exchange rate would affect net earnings by approximately 20¢ per common share.

Working capital at December 31, 1978 amounted to $300.7 million and current assets were 2.6 times current liabilities. Net cash resources at the end of the year amounted to $52.3 million, an increase of $30.5 million over the previous year.

Capital expenditures in 1978 amounted to $59.2 million and planned expenditures for 1979 are $130 million.

On October 13, 1978, Abitibi purchased 1,010,996 common shares of The Price Company Limited from Consolidated-Bathurst Inc. for $23.00 per share and on October 25 a similar offer was made to the remaining common shareholders of Price. At the year-end Abitibi owned 98.6% of the common shares of Price and has since commenced proceedings under Section 48 of The Quebec Companies Act to acquire the remaining common shares. This additional investment in Price was largely financed by the issue in mid-November, through a wholly-owned subsidiary of Abitibi, of $75 million of floating-rate term preferred shares to institutional investors.

As a result of acquiring most of the remaining outstanding common shares of Price during 1978, the major part of the minority shareholders' interest of $23,276,000 appearing on the balance sheet now represents The New York Times' 49% investment in Price's subsidiary company, Gaspesia Pulp and Paper Company Ltd.

On December 21, 1978, Abitibi purchased all of the outstanding shares of Labrador Linerboard Limited from the Province of Newfoundland for $43.5 million and commenced proceedings to wind up the company into Abitibi. The principal asset of the company was the idle linerboard mill located at Stephenville, Newfoundland and, as part of the agreement, Abitibi undertook to convert the mill to a 150,000 ton per year newsprint facility. The conversion project is estimated to cost $60 million over a two-year period, with initial production of newsprint scheduled for late 1980. The Department of National Revenue has confirmed the availability to Abitibi of approximately $205 million of unused capital cost allowances relating to the original linerboard mill. The resulting tax reductions of approximately $90 million, in combination with a $15 million DREE grant towards the conversion project, will offset the cost involved in establishing a competitive newsprint mill at Stephenville and will benefit earnings commencing with the successful start-up of the new facility.

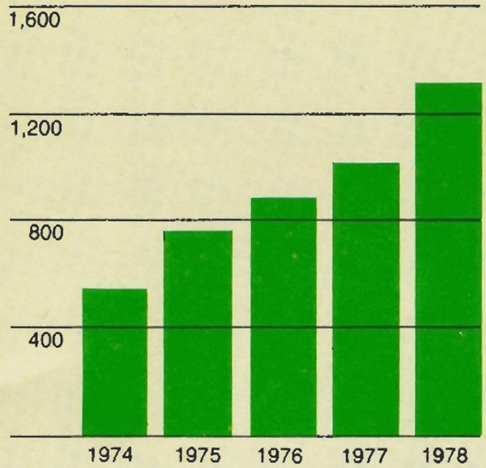
As announced midway through the year, effective July 1, 1978, Abitibi purchased Price's wholly-owned subsidiary, Price Wilson Limited, which is engaged in the distribution of converted paper products and which had been incurring continuing losses in recent years. Price Wilson was subsequently merged with Inter City Papers Ltd., a wholly-owned subsidiary of Abitibi, which carries on a fine paper distribution business with a proven record of profitability. In management's opinion this was the only way to reverse Price Wilson's loss trend and to provide an opportunity for profitable growth as well as some synergistic gains. Based on a valuation received from an independent management consulting firm retained by Price, the purchase price was set at $7.3 million and, after allowing for the minority shareholders' portion of Price's loss on the transaction, an amount of $3 million was written off as an extraordinary item in Abitibi's consolidated accounts in order to reduce Price Wilson's net assets to their approximate market value.

As a result of federal tax changes introduced in 1977, Abitibi was able to proceed with the dissolution and amalgamation of certain subsidiary companies and use virtually all of the prior years' tax losses of the Abitibi/Price group in 1978. The resulting tax reductions of $2,695,000 net of minority interest, have been included in extraordinary items on the earnings statement.

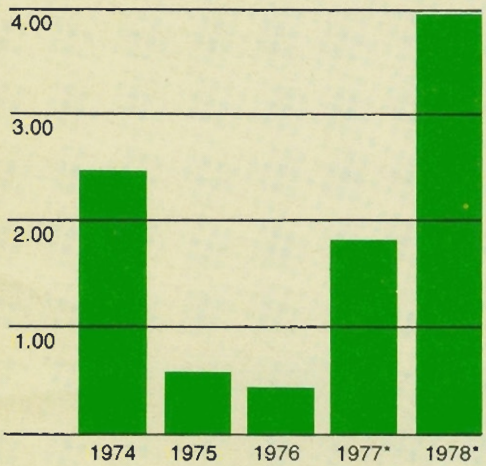
The federal government's investment tax credit program for qualified capital investments in Canada, previously referred to, in addition to similar credits in respect of U.S. operations and the 3% federal inventory allowance have increased 1978 earnings by approximately $4.3 million, as compared with $2.8 million in 1977.

Studies aimed at developing accounting standards which will reflect realistically the effects of inflation continue to be carried out by the accounting profession. As no generally accepted method of accounting for the effects of inflation has yet been developed, Abitibi continues to report its financial results on the conventional historical basis, which overstates profits during periods of inflation. In particular, it should be recognized by governments, employees and shareholders alike that depreciation based on the historical cost of assets is inadequate to provide for their replacement.

Net Sales
(millions of dollars)

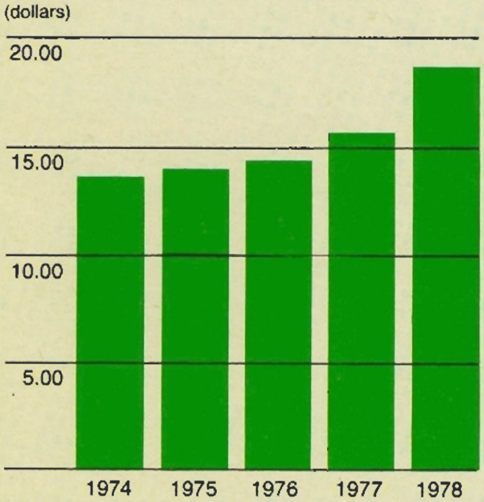


Earnings Per Common Share
(dollars)



*before extraordinary items

Book Value Per Common Share
(dollars)



Net Sales by Product
(thousands of dollars)

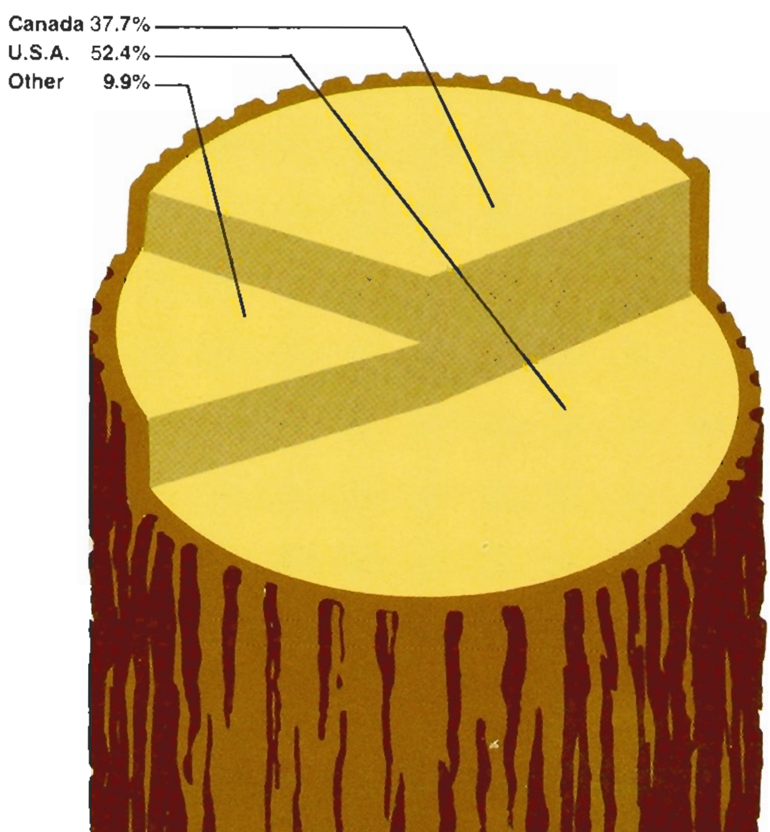
	1978	1977
Newsprint	$ 615,257	$ 496,940
Uncoated groundwood papers	105,235	71,703
Fine papers, including merchant and converting operations	268,160	218,208
Building products and packaging	164,756	147,376
Paperboard, kraft paper and pulp	47,064	47,982
Lumber	95,227	60,850
	$1,295,699	$1,043,059

Net Sales and Earnings by Quarter
(thousands of dollars)

	Net Sales		Earnings	
	1978	1977	1978	1977
1st quarter	$ 292,129	$ 232,681	$14,766*	$ 3,486
2nd quarter	327,647	255,177	17,104*	6,844
3rd quarter	337,205	270,602	22,459*	11,242*
4th quarter	338,718	284,599	24,321*	16,336*
	$1,295,699	$1,043,059	$78,650*	$37,908*

*before extraordinary items

Net Sales by Market—1978



Consolidated Net Earnings

(thousands of dollars except per share calculations)

	Year Ended December 31 1978	1977 (Note 18)
Sales, less delivery expenses	$1,295,699	$1,043,059
Other income (note 3)	6,645	5,712
	1,302,344	1,048,771
Cost of sales	990,317	830,264
Selling, general and research expenses	83,872	76,724
Depreciation and depletion	48,307	43,963
Interest and expense on long-term debt	23,173	22,742
Other interest	645	1,114
Income taxes	63,738	29,363
	92,292	44,601
Mining income (note 4)	2,478	3,283
Interest in earnings of non-mining companies accounted for on the equity basis (note 5)	2,184	1,647
	96,954	49,531
Minority shareholders' interest	18,304	11,623
Earnings before extraordinary items	78,650	37,908
Extraordinary items (note 6)	305	1,687
Net earnings	$ 78,345	$ 36,221
Per common share		
Earnings before extraordinary items	$ 3.98	$ 1.83
Net earnings	3.96	1.74

Consolidated Retained Earnings

(thousands of dollars)

	Year Ended December 31 1978	1977
Retained earnings at beginning of year	$ 237,600	$ 212,191
Net earnings	78,345	36,221
	315,945	248,412
Dividends declared—preferred shares	4,703	4,366
—common shares	17,680	6,446
Retained earnings at end of year	$ 293,562	$ 237,600

Changes in Consolidated Financial Position

(thousands of dollars)

	Year Ended December 31 1978	1977
Financial Resources Provided By:		
Earnings before extraordinary items	$ 78.650	$ 37.908
Charges (credits) to earnings not affecting working capital:		
Depreciation and depletion	48,307	43,963
Deferred income taxes	3,385	6,063
Interest in earnings of companies accounted for on the equity basis–		
Mattabi Mines Limited	(3,280)	(3,421)
Other	(2,184)	(1,647)
Minority shareholders' interest	18,304	11,623
Other–net	(58)	(927)
Funds from operations	143,124	93,562
Extraordinary items–net	655	376
Issue of preferred shares of a subsidiary company	75,000	–
Convertible promissory notes	27,500	–
Deferred income	23,355	–
Dividends from Mattabi Mines Limited	4,800	6,000
Disposals of fixed assets	1,792	4,114
Decrease in receivables not currently due	1,121	1,793
Issue of common shares	2	4,823
Other items–net	1,562	(837)
	278,911	109,831
Financial Resources Used For:		
Acquisition of shares of–		
The Price Company Limited	95,520	4,823
Labrador Linerboard Limited, net of working capital acquired	40,900	–
Additions to fixed assets	59,163	43,580
Dividends		
Shareholders of the Company	22,383	10,812
Minority shareholders of subsidiary companies	4,945	1,640
Reduction of long-term debt net of unrealized exchange loss	11,976	11,526
Retirement of preferred shares	2,097	2,183
Acquisitions (disposals) of investments	1,090	(7)
	238,074	74,557
Increase in Working Capital	40,837	35,274
Working Capital at Beginning of Year	259,836	224,562
Working Capital at End of Year	$300,673	$259,836

Consolidated Balance Sheet

(thousands of dollars)

ASSETS

	December 31 1978	December 31 1977
Current Assets:		
Cash and short-term investments	$ 57 733	$ 29.178
Accounts receivable	199.726	166 322
Inventories (note 7)	222.064	201.228
Prepaid expenses	5.586	4.867
	485 109	401 595
Fixed Assets:		
Properties, plant and equipment	883.056	808 133
Logging equipment and development	60.135	47.918
Woodlands and mining and water power rights	44.601	43.499
	987,792	899.550
Less—accumulated depreciation and depletion	468.381	423.320
	519.411	476.230
Other Assets:		
Equity interests		
Mattabi Mines Limited (note 4)	13.461	14.981
Other companies (note 5)	7.845	5.708
Receivables not currently due	2.417	3.538
Investments (note 8)	5.933	5.236
Cost of shares of acquired companies in excess of values attributed to underlying net assets, less accumulated amortization	20.080	20,129
Unamortized discount and expense on long-term debt	1.368	1 524
Unrealized loss on translation of long-term debt payable in U S funds (note 1(b))	16.839	6.210
	67.943	57.326
	$1.072.463	$935.151

The financial statements have been approved by the Board

T. J Bell, Director

R C. Gimlin, Director

LIABILITIES	December 31 1978	1977
Current Liabilities:		
Bank indebtedness	$ 5,446	$ 7,411
Accounts payable and accrued liabilities	131,415	104,870
Income and other taxes payable	18,602	15,930
Dividends payable	8,082	3,276
Long-term debt due within one year (note 9)	10,891	10,272
Promissory notes (note 2(b))	10,000	–
	184,436	141,759
Convertible Promissory Notes (note 2(b))	27,500	–
Deferred Income (note 2(b))	23,355	–
Long-Term Debt (note 9)	241,165	242,512
Deferred Income Taxes	106,628	103,224
Minority Shareholders' Interest	23,276	110,417
SHAREHOLDERS' EQUITY		
Preferred Shares Issued by a Subsidiary Company (note 10)	75,000	–
Preferred Shares (note 11)		
Authorized: 1,000,000 shares par value $50 issuable in series (1,000,000 shares issued; 145,710 shares redeemed)		
Outstanding: 174,290 7½% Cumulative Redeemable Preferred Shares, Series A (1977–176,290 shares)	8,715	8,815
680,000 10% Cumulative Redeemable Preferred Shares, Series B (1977–720,000 shares)	34,000	36,000
Common Shares (note 12)		
Authorized: 24,000,000 shares without nominal or par value		
Issued 18,668,244 shares (1977–18,547,076 shares)	54,826	54,824
Retained Earnings	293,562	237,600
	466,103	337,239
	$1,072,463	$935,151

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

(a) Principles of Consolidation

The consolidated financial statements include the accounts of Abitibi Paper Company Ltd. and all companies in which it holds more than a 50% interest. Investments in companies in which Abitibi holds a major interest, but not more than 50%, are included in the consolidated financial statements in accordance with the equity method of accounting.

The cost of shares of acquired companies in excess of values attributed to underlying net assets is recorded as an asset on the consolidated balance sheet. The excess for companies acquired prior to 1974 is not being amortized, while the excess in respect of subsequent acquisitions is amortized on a straight-line basis over an appropriate period not in excess of 40 years.

(b) Translation of Foreign Currencies

Balances and transactions in other currencies have been translated into Canadian dollars as follows:

Fixed assets, investments and deferred income taxes at historical rates of exchange.

Other assets and liabilities at rates in effect at December 31.

Items included in net earnings at rates prevailing during the year, except depreciation and depletion which are on the same basis as the related fixed assets.

In September 1978 the Canadian Institute of Chartered Accountants published recommendations covering the translation of foreign currency transactions and foreign currency financial statements which are effective for financial years commencing on or after December 1, 1978 and, accordingly Abitibi will adopt the recommendations in its 1979 fiscal year. The only recommendation which will have an effect of any consequence on Abitibi earnings concerns gains or losses arising from the translation of long-term debt payable in foreign currencies. It has been Abitibi's practice to defer such gains or losses until realized, whereas in future they will be amortized to earnings over the lifetime of the debt. Had the new C.I.C.A. recommendations been adopted in 1978, Abitibi's net earnings would have been reduced by approximately $2.5 million for that year and comparative 1977 earnings would have been reduced by approximately $1.2 million.

(c) Inventories

Inventories of finished products, work in process and materials and operating supplies are valued at the lower of average cost and net realizable value. Inventories of pulpwood and sawlogs are valued at average cost.

(d) Fixed Assets and Depreciation

Fixed assets are recorded substantially at cost and depreciation is provided at rates considered adequate to amortize the cost over the productive lives of the assets. The principal asset category is primary production equipment which is depreciated over 20 years on a straight-line basis. Timber limits are depleted on the unit-of-production basis to the extent of amounts allowable for income tax purposes.

(e) Discount and Expense on Long-Term Debt

Discount and expense on long-term debt is amortized over the terms of the related obligations.

(f) Research and Development

Research and development expenditures are written off when incurred, except for expenditures on physical facilities which are capitalized and depreciated on a straight-line basis over their estimated useful lives.

(g) Pension Costs

Current service pension costs are charged to earnings and funded as they accrue. Past service costs are charged to earnings and funded at rates which, based on independent actuarial estimates, will fully provide for the obligations over periods not longer than those permitted by the various regulatory bodies.

(h) Income Taxes

Earnings are charged with income taxes relating to reported profits. Differences between such taxes and taxes currently payable, which result from timing differences between the recognition of income and expenses for accounting and for tax purposes, are reflected as Deferred Income Taxes in the financial statements.

When losses are incurred, no provision is made for the related tax benefit unless recovery is virtually certain. When tax benefits not previously recognized are realized they are included in earnings as an extraordinary item.

Investment tax credits are accounted for using the "flow-through" method which recognizes the tax benefit in the year the eligible capital expenditures are made.

(i) Earnings Per Common Share

Earnings per common share calculations are based on the average number of shares outstanding during the year and are computed after allowing for dividends on preferred shares

2. Acquisitions

(a) The Price Company Limited

On October 13, 1978 Abitibi purchased 1,010,996 common shares of Price from Consolidated-Bathurst Inc. for $23 per share and a further 3 114,580 shares were acquired from Price's remaining common shareholders following a cash offer made on October 25 at the same price. At December 31, 1978 Abitibi owned 9 897,727 or 98.6%, of the 10 037,761 outstanding common shares of Price

(b) Labrador Linerboard Limited

On December 21 1978 Abitibi purchased all of the outstanding shares of Labrador Linerboard from the Province of Newfoundland for $43 5 million and commenced proceedings to wind up the Company into Abitibi The acquisition was accounted for using the purchase method and the purchase price has been allocated as follows:

Working capital	$ 2,600,000
Fixed assets, consisting primarily of the idle linerboard mill at Stephenville, Nfld	40,900,000
Total	$43,500,000

Consideration for the purchase consisted of $6 million cash and $37 5 million of non-interest bearing promissory notes maturing on December 31, 1979. At Abitibi's option, $27.5 million of the notes may be settled at maturity through the issuance of non-dividend bearing preferred shares, one-quarter of which would be redeemed at par on December 31 in each of the years 1981 to 1984

As a condition to the agreement, Abitibi will convert the existing linerboard mill to a 150,000 ton per year newsprint mill, with production to commence prior to October 1981. It is estimated that the conversion will cost $60 million, in connection with which a federal Department of Regional Economic Expansion grant of $15 million has been approved

The Department of National Revenue has confirmed the availability to Abitibi of approximately $205 million of unused capital cost allowances which apply to the original linerboard mill. As the related tax reductions are realized, it is Abitibi's intention to treat them as Deferred Income, which will be utilized to offset preproduction and start-up costs, with the balance to be transferred to earnings over the productive life of the new newsprint mill At December 31, 1978 such deferred income amounted to $23,355,000.

3. Other Income

	1978	1977
Interest and miscellaneous income	$ 6,844,000	$ 4,401,000
Gain (loss) on current maturities of long-term debt	(258,000)	241,000
Net gain on disposals of fixed assets and investments	59 000	1,070,000
	$ 6,645,000	$ 5,712,000

4. Mining Income

	1978	1977
Equity in earnings of Mattabi Mines Limited	$ 3,280,000	$ 3,421,000
Mining loss of The Price Company Limited	(802,000)	(138,000)
	$ 2,478,000	$ 3,283,000

	1978	1977
Equity in Mattabi Mines Limited		
Equity at beginning of year	$14,981,000	$17,560,000
Equity in earnings	3,280,000	3,421,000
	18,261,000	20,981,000
Dividends received	4,800,000	6,000,000
Equity at end of year	$13,461,000	$14,981,000

5. Equity Interest—Other Companies

	1978	1977
Equity at beginning of year	$ 5,708,000	$ 4,326,000
Equity in earnings	2,184,000	1,647,000
Additional investment	–	50,000
	7,892,000	6,023,000
Dividend received	17,000	15,000
	7,875,000	6,008,000
Loss on disposal of investment	30,000	300,000
Equity at end of year	$ 7,845,000	$ 5,708,000

6. Extraordinary Items

	1978	1977
Writedown of Price Wilson Limited net assets to approximate market value*	$ 3,000,000	$ –
Loss on disposals of investments and assets in subsidiary companies in 1977, net of minority interest of $1,472,000	–	2,337,000
Less:		
Income tax reductions realized on utilization of losses incurred in prior years by subsidiary companies, net of minority interest (1978–$1,272,000; 1977–$347,000)	2,695,000	650,000
	$ 305,000	$ 1,687,000

*Effective July 1, 1978, Abitibi purchased The Price Company Limited's wholly-owned subsidiary, Price Wilson Limited, and subsequently merged it with Inter City Papers Ltd., a wholly-owned subsidiary of Abitibi. Based on a valuation received from an independent management consulting firm retained by Price, the purchase price was established at $7.3 million. Price incurred a loss of $5,172,000 on the transaction, of which $2,172,000 was allocated to the minority interest and the balance of $3,000,000 was written off in Abitibi's consolidated accounts in order to reduce Price Wilson's net assets to their approximate market value.

7. Inventories

	1978	1977
Finished products and work in process	$ 66,221,000	$ 62,598,000
Pulpwood, sawlogs and expenditures on current logging operations	102,630,000	89,165,000
Materials and operating supplies	53,213,000	49,465,000
	$222,064,000	$201,228,000

8. Investments, at cost

	1978	1977
Bonds, debentures and notes	$ 1,058,000	$ 1,059,000
Townsite mortgages and advances	1,860,000	1,902,000
Other	3,015,000	2,275,000
	$ 5,933,000	$ 5,236,000

9. Long-Term Debt	1978	1977
Abitibi Paper Company Ltd.		
Sinking Fund Debentures—		
5¼% Series A maturing 1985	$ 11,977,000	$ 11,952,000
7¼% Series B maturing 1987	9,492,000	10,494,000
9¾% Series D maturing 1990	11,940,000	12,749,000
10½% Series E maturing 1995	42,500,000	42,500,000
11% Series F maturing 1995	14,210,000	14,500,000
11⅜% Series G maturing 1995	71,148,000	65,640,000
Abitibi Corporation and subsidiary companies:		
Revolving Bank Credit, maximum interest ⅝% above lender's prime rate	9,486,000	8,752,000
Instalment Note bearing interest at ⅝% above lender's prime rate maturing 1981	2,668,000	3,282,000
5⅛% Instalment Notes maturing 1984	7,115,000	7,330,000
5½% Instalment Note maturing 1986	9,486,000	9,846,000
7⅜% Instalment Notes maturing 1988	14,230,000	14,222,000
5¼% Instalment Note maturing 1991	3,297,000	3,209,000
Miscellaneous notes	3,723,000	4,212,000
The Price Company Limited and subsidiary companies:		
Sinking Fund Debentures—		
5¾% Series A maturing 1982	7,500,000	8,700,000
6¾% Series B maturing 1987	18,300,000	19,600,000
5½% Sinking Fund Notes maturing 1985	9,237,000	9,736,000
6% Subordinated Sinking Fund Notes maturing 1986	4,364,000	4,551,000
Other indebtedness	1,383,000	1,509,000
	252,056,000	252,784,000
Less: Amount due within one year	10,891,000	10,272,000
	$241,165,000	$242,512,000

Sinking fund and instalment payment obligations for 1979 amount to $12,391,000 of which $1,500,000 has been discharged by prior purchase and retirement. Principal repayment obligations for the years 1980 to 1983 are estimated to be $13,500,000, $18,000,000, $19,800,000 and $16,500,000, respectively. Long-term debt payable in U.S. dollars included above aggregated $123,740,000 U.S. at December 31, 1978 (1977—$130,469,000 U.S.).

Abitibi Paper Company Limited has effectively guaranteed payment of certain outstanding long-term debt of Abitibi Corporation and subsidiary companies amounting to $28,250,000 U.S. at December 31, 1978.

10. Preferred Shares Issued by a Subsidiary Company

On November 16, 1978 a wholly-owned subsidiary company of Abitibi issued 1,500,000 Preferred Shares Series A, at a price of $50 per share, for a total consideration of $75,000,000. Terms attaching to the preferred shares provide for a dividend rate floating at one-half the average prime rate of the five largest Canadian chartered banks plus 1%, payable quarterly. The shares are retractable at the option of the holders at $50 at the end of 10 years and they are redeemable by the company at $50 plus accrued and unpaid dividends after January 1, 1981. In the event of the non-fulfilment of certain conditions attaching to the shares, the holders have the right to receive from Abitibi, at its option, cash or equivalent preferred shares of Abitibi.

11. Preferred Shares

The Series A shares are redeemable at the option of Abitibi at $52 per share up to May 31, 1983 and at $51 per share thereafter. During 1978, 2,000 Preferred Shares, Series A with a par value of $100,000 (1977—4,020 shares with a par value of $201,000) were purchased and cancelled pursuant to the conditions attaching to this series.

The Series B shares are redeemable at par through the operation of a cumulative sinking fund at the rate of 40,000 shares annually. The Series B shares are otherwise redeemable at $52.50 per share up to June 15, 1981 and at declining prices thereafter. During 1978, 40,000 Preferred Shares, Series B with a par value of $2,000,000 were redeemed pursuant to the conditions attaching to this series.

12. Common Shares

Of the authorized and unissued common shares, 658,844 shares are reserved under the Key Employees' Stock Option Plan and options are outstanding on 413,734 shares at prices equal to market value at date of grant ranging from $7.3125 to $12.625 per share, of which options in respect of 306,178 shares are held by senior officers of Abitibi. Options are for terms of up to ten years and are exercisable mostly in instalments upon fulfilment of service conditions.

The Plan was amended in 1973 to provide for the use of a market growth formula at date of exercise for all subsequent options and to permit this as an alternative for options then outstanding. In accordance with this formula, the market growth amount is determined by multiplying the number of shares with respect to which the option is exercised by the excess of market value per share at date of exercise over market value at date of grant. Shares to this value are issued in consideration of the relinquishment by the optionee of his option right to the remaining shares in the calculation of the market growth amount and the payment of one cent per share issued.

There were 121,168 shares issued in 1978 (1977—267 shares) under the terms of the Plan.

13. Capital Projects

An estimated $85 million will be required to complete approved capital projects, excluding the commitment to convert the Stephenville, Nfld. linerboard mill to a newsprint mill as referred to in Note 2(b).

14. Lease Obligations

Abitibi and its subsidiaries are committed under leases, principally for office and warehouse premises and woods equipment, for varying terms expiring up to 1999. The aggregate rental payments required for the 12 months ending December 31, 1979 under leases having an unexpired term of more than one year at December 31, 1978 are $4,500,000, of which $2,500,000 is attributable to leases having an unexpired term of more than five years.

15. Unfunded Pension Benefits

The most recent independent actuarial estimates, which include the effect of improvements made to pension plans during 1978, indicate that the single-sum liability for unfunded past service pension benefits not provided for in the accounts at December 31, 1978 is approximately $50 million.

16. Anti-Inflation Program

Abitibi and its Canadian subsidiaries were subject to controls on prices, profits, compensation and dividends under the federal government's anti-inflation program and have complied with that program.

17. Other Statutory Information

(a) Remuneration in 1978 of Abitibi's 16 directors and 37 officers, including past officers, determined in accordance with the Canada Corporations Act, amounted to $70,000 and $2,782,000, respectively. Five officers of Abitibi served also as directors.

(b) Loans outstanding with officers relating to the purchase of residences amounted to $428,000 at December 31, 1978.

18. Reclassification

For purposes of uniformity, certain warehousing costs previously included in selling expenses are now treated as delivery expenses and comparative 1977 figures have been reclassified accordingly.

Auditors' Report

To the Shareholders of ABITIBI PAPER COMPANY LTD.:

We have examined the consolidated balance sheet of Abitibi Paper Company Ltd. as at December 31, 1978 and the consolidated statements of net earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances. We have relied on the reports of other independent accountants who have examined the financial statements of two partly-owned companies accounted for by the equity method.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

PRICE WATERHOUSE & CO.
Chartered Accountants

Toronto, February 14, 1979

Five Year Review

(thousands of dollars except per share calculations)

	1978	1977	1976	1975	1974
Sales and Earnings:					
Sales less delivery expenses	$1,295,699	$1,043,059	$880,351	$764,384	$551,893
Depreciation and depletion	48,307	43,963	41,942	42,071	21,243
Interest expense	23,818	23,856	25,032	22,505	9,398
Income taxes	63,738	29,363	13,483	15,141	30,099
Mining income	2,478	3,283	3,844	5,307	10,257
Minority shareholders' interest	18,304	11,623	3,687	7,428	1,295
Earnings before extraordinary items	78,650	37,908	13,024	13,985	45,880
Per common share	$ 3.98	$ 1.83	$ .47	$ .63	$ 2.50
Extraordinary items	305	1,687	—	—	
Net earnings	78,345	36,221	13,024	13,985	45,880
Per common share	$ 3.96	$ 1.74	$ .47	$ .63	$ 2.50
Dividends Declared:					
Preferred shares	$ 4,703	$ 4,366	$ 4,584	$ 2,622	$ 718
Common shares	17,680	6,446	2,172	7,239	11,763
Per common share	$ .95	$ .35	$ .12	$ .40	$ .65
Additions to Fixed Assets	$ 59,163	$ 43,580	$ 54,371	$ 71,041	$ 35,460
Financial Position:					
Working capital	$ 300,673	$ 259,836	$224,562	$229,023	$ 87,948
Net fixed assets	519,411	476,230	489,437	478,205	452,985
Long-term debt	241,165	242,512	243,168	255,522	139,163
Deferred income taxes	106,628	103,224	99,725	91,299	80,940
Minority shareholders' interest	23,276	110,417	111,671	108,090	110,795
Preferred shares	117,715	44,815	47,016	49,261	9,469
Book value of common shares	348,388	292,424	262,192	255,924	252,890
Per common share	$ 18.66	$ 15.77	$ 14.49	$ 14.14	$ 13.97

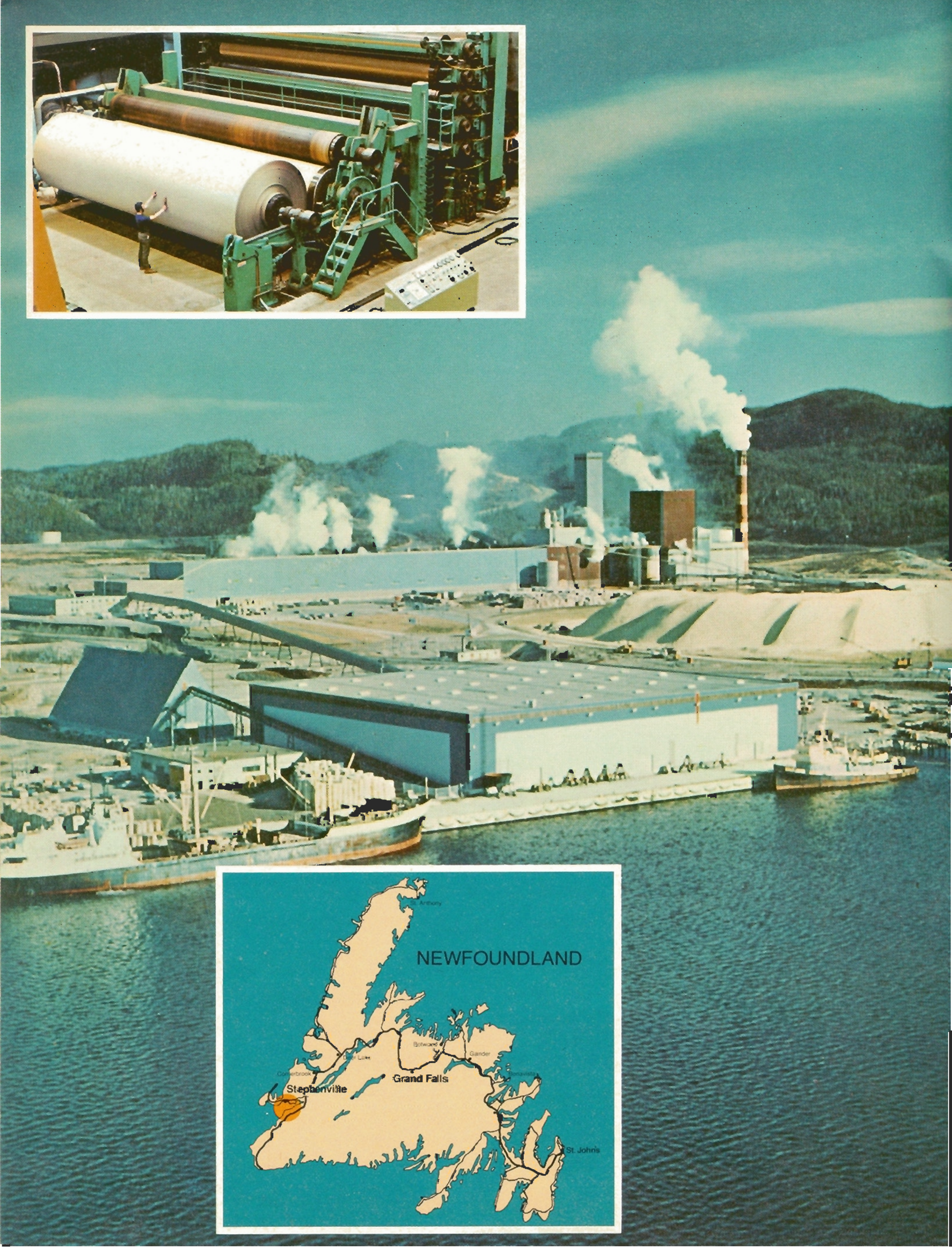
Primary Production

		Newsprint	Uncoated Groundwood Papers	Fine and Printing Papers	Building Boards	Paperboards Kraft Paper and Market Pulp	Lumber
		Tons	Tons	Tons	Msf	Tons	Mfbm
Capacity	**1978**	1,998,000	298,000	182,000	987,000	318,000	441,000
Production	**1978**	1,962,000	292,000	181,000	935,000	297,000	356,000
	1977	1,694,000	231,000	157,000	904,000	271,000	324,000
	1976	1,711,000	211,000	113,000	854,000	247,000	272,000
	1975	1,548,000	129,000	77,000	733,000	162,000	130,000
	1974	2,011,000	277,000	183,000	738,000	315,000	237,000

(a) Capacity figures indicate effective annual output and generally are somewhat less than rated capacities due to allowances for items such as maintenance downtime

(b) A significant portion of Abitibi's market pulp production (more than 60% in 1978) is consumed in the manufacture of primary paper products at other Abitibi mills

(c) Building board production is expressed on an equivalent thickness basis


NEWFOUNDLAND
St. Anthony
Botwood
Gander
Bonavista
Grand Falls
Stephenville
St. Johns

Newsprint

Charles R. Tittemore

Bernd K. Koken

K. Linn Macdonald

1978 went into the records as a banner year for Canadian newsprint manufacturers—consumption in Canada and in all markets to which Canada exports was exceptionally strong, thereby creating a demand on Canadian mills to run at near-capacity in order to supply requirements that could not be met by home producers. U.S. consumption rose 6.4% over 1977, reflecting increased advertising lineage, a continuation of the trend toward advertising and special interest inserts and newspaper circulation gains. Similarly, Canadian demand was 10% ahead of 1977, offsetting a 3% decline in shipments to offshore markets.

Strikes at U.S. West Coast mills in addition to a few isolated labour interruptions at Canadian operations combined to place an even greater strain on supply in the second half. Only a small part of strike-induced production losses was offset by lower demand as a result of the prolonged strikes at newspapers in New York and elsewhere. Year-end inventories held by consumers and producers were lower than 1977 levels.

Canadian industry production totalled 9.8 million tons, representing an 8.7% gain over 1977 and a 98% operating rate. Production at Abitibi's mills was 1.96 million tons which resulted in an operating rate of 99%. During the year the Kenogami mill ceased newsprint production as part of the program to dedicate the mill to uncoated groundwood papers.

Progress was made in 1978 in the planned program to modernize manufacturing facilities and to upgrade quality to meet the more stringent requirements of higher-speed presses and advanced printing processes. Additional expenditures were directed toward manufacturing cost reductions, and to Abitibi's ongoing commitment to environmental improvements at its mill sites. The newsprint capital expenditure program for 1979 will continue to be directed toward these targets, but at a dramatically accelerated pace. The program will include computerized control systems on paper machines to improve product uniformity, increased use of refuse as fuel to reduce energy costs, furnish treatment to provide improved offset newsprint, and the first stage of an $18 million program to replace the sulphite pulp at the Fort William mill, significantly reducing BOD demand of the mill effluent.

Stephenville Division

In December the company completed the acquisition from the Newfoundland Government of its Crown Corporation, Labrador Linerboard Limited and its primary asset, a linerboard mill located at Stephenville on the West Coast of Newfoundland. Engineering is underway for the conversion of the mill to newsprint manufacture by late 1980. Total cost of the project will approximate $100 million, and completion of the conversion will add to the newsprint group a mill that is thoroughly modern with respect to both production facilities and the environment, and one which will enable the company to enhance its service to both the offshore and North American markets.

The outlook for 1979 is optimistic. Given the consensus forecast of a mild recession in the U.S. economy by mid-year, consumption in that market will remain at, or somewhat above, the 1978 experience. Modest growth is predicted in the Canadian market and overseas demand is expected to match that of 1978. Although new capacity will come on stream in 1979, supply and demand will be in reasonable balance and Abitibi expects operating rates to be adequate. Abitibi-Price has announced a $25 per ton increase, effective March 1, 1979, in its price of newsprint shipped to the U.S. which will recover anticipated cost increases.

Outlook Beyond 1979

As noted previously, 1979 is projected to repeat 1978's performance in terms of newsprint margins and operating rates. It is almost certain, also, that a large share of 1979 earnings will be attributable to the Canadian dollar exchange rate, which enables the Canadian industry to be competitive in export markets. This situation could extend beyond 1979, providing the industry with an opportunity to maintain its competitiveness as a world supplier of newsprint by making investments directed at improving productivity and reducing costs.

During the years 1980-82, announced new capacity coming on stream in the U.S. should at least match increased demand and perhaps exceed it. Should demand growth falter and capacity growth further accelerate, the Canadian industry could be faced with some less than capacity operating rates during this 2-3 year period.

Newsprint

The $60 million project to convert the Stephenville mill to a modern newsprint facility with an annual capacity of 150,000 tons is well into the planning stage. Start-up is scheduled for late 1980.

The Abitibi-Price long range plan is directed toward applying the cash flow generated by the current strong situation to specific opportunities that have been identified to reduce costs and improve productivity and quality in order to compete more effectively with the new facilities being installed principally in the U.S.

To achieve the goal of returning the Canadian newsprint manufacturing industry to an internationally competitive position, requires a widespread recognition of the importance of this industry to the Canadian economy and a dedication to achieving this goal. Labour, governments and the public at large, must all take positions consistent with this priority.

Uncoated Groundwood Papers

Formed as a separate business unit in 1977 the uncoated groundwood papers group progressed at an encouraging rate in 1978, with strong demand experienced in all product lines. This plus major improvements in product development, quality and production, as well as a well-orchestrated approach to the market, have served to place Abitibi in the role of a major supplier of rotogravure, directory, offset and other groundwood-based specialties to commercial printers in North America.

Except for a brief strike at one location, both of the group's mills at Sault Ste. Marie, Ontario and Kenogami, Quebec operated at 100% of capacity in 1978 and produced 292,000 tons. Uncoated groundwood paper is now one of the larger contributors to sales revenue within Abitibi.

During 1978, two machines at Kenogami ceased newsprint production and were switched to uncoated groundwood grades several months ahead of plan. The $32 million capital program to complete the conversion of Kenogami to the TCMP process and 100% groundwood papers got underway in early 1978 and is proceeding on schedule. Completion is targetted for 1980, by which time Abitibi will become North America's largest producer of these grades for the fast-growing market.

In the meantime, the outlook for 1979 is favourable and the mills are expected to again operate at full capacity.

John G. Davis

Fine Papers

A resurgence in demand for fine papers, coupled with diminishing imports from the U.S. highlighted 1978 for the Canadian fine paper industry, and all facets of Abitibi's fine papers business made impressive gains.

Manufacturing

Abitibi-Provincial, as did other Canadian fine paper manufacturers, experienced a significant rebound from the strike-induced industry depression of 1976-77. Canadian demand for printing and writing papers rose an unusual 18% during the year, creating a return to a healthy backlog position, and improved pricing patterns. Additionally, the market was stabilized for Canadian producers by the substantial reduction in imports from the U.S., brought about in part by increased home demand and the discounted Canadian dollar.

An optimistic picture emerges when 1979 sales forecasts are matched against Canadian supply levels. This is further enhanced by forecasts that the Canadian dollar exchange rate and tariffs will continue to minimize imports.

Nevertheless Abitibi-Provincial is preparing for profitability in an environment which is likely to include reduced tariff protection and a less advantageous exchange rate. Strategies are in place that will see further capital being invested to continue improving mill operating efficiencies, equipment optimization and product consistency. For the longer term, plans focus on a rationalized grade structure which concentrates Abitibi-Provincial's marketing and capital programs on products in which the company has inherent advantages. Thus Abitibi-Provincial views the future with some optimism.

Inter City Papers Limited and Subsidiaries

1978 was the most successful year in the company's history with all traditional operations of Inter City contributing, particularly the major divisions in Montreal and Toronto. During 1978 Hillier Paper Limited became Inter City Papers (Manitoba) Limited and Price Wilson Limited became a division of the company following its acquisition by Abitibi from The Price Company Limited.

Price Wilson

The program to divest non-profitable operations was concluded with the sale of

Woodlands

The raw products of the forest, logs and wood chips, are the resource base from which Abitibi manufactures its paper and lumber product mix. The company's strategy is targetted on improved forest management and utilization practices, and increased mechanization.

Texport which leaves Price Wilson with a solid core of its traditionally successful activities in converting and distribution. Moreover, costs have been reduced and expertise has been developed in previously critical areas. The synergies of Price Wilson's integration into Inter City should begin to take effect in 1979. The 1979 outlook for Inter City and its subsidiaries is for continued growth in both sales and earnings.

Hilroy Ltd.

Bolstered by an improved share of certain stationery markets, and by measurable improvements in efficiency and productivity, Hilroy's higher level of sales in 1978 resulted in earnings returning to a satisfactory level.

Hilroy experienced substantial increases in the cost of its raw material in 1978 and expects this trend to continue in 1979. However, the reorganization and integration of Hilroy and its subsidiary Papeterie Canadienne that was completed in 1978, and the introduction of new products and merchandising concepts, are expected to contribute to a further improvement in performance in 1979.

Canada Envelope Company

The company topped its 1977 records in sales and earnings with its plants in Vancouver, Calgary, Winnipeg, Toronto and Stellarton all contributing. Canada Envelope entered 1979 with a continuation of the good backlogs of 1978 which is promising.

Building Products and Packaging

Charles F. Buckland

U.S. Building Products

With single family housing starts at a record level in 1978 and with continued vigour in remodeling and repair, Abitibi's U.S. Building Products divisional sales were at a record level in 1978. Particularly strong were sales of the company's exterior products, siding and sheathing, manufactured respectively at Roaring River, North Carolina, and Blountstown, Florida, but due to softened demand in the second half of the year, sales of prefinished panelling and moulding were mixed. Competitive pressures in this latter market made it impossible to raise prices sufficiently to offset cost increases although we did make gains in productivity and energy conservation. Because of the proportionate role of panelling and mouldings in the division's activities, earnings in U.S. dollars were below those of 1977 although there was a year to year gain on translation to Canadian dollars.

Consistent with its dedication to design leadership, the division's continuing high level of R&D produced 18 new panelling products as sales stimulants in 1978. Additionally, a promising new moulding product is being test-marketed which is expected to make substantial inroads into the market and to favourably impact 1979 sales and earnings performance.

A major step in the division's plan for modernization and rationalization will be taken in April 1979 when the new Toledo, Ohio panel prefinishing operation begins production of more sophisticated panel designs. A $22 million capital program at the Roaring River, North Carolina exterior siding plant will begin in 1979 and will see the resulting 50% capacity increase by early 1981 being timed to maintain Abitibi's share of the market foreseen for the early 1980's.

The division's outlook for 1979 is uncertain. U.S. housing starts are projected to retract to 1.7 million; it is too early to predict the effect on inflation of voluntary wage and price guidelines; and therefore the course that may be taken by the Administration in influencing the path of the U.S. economy is unclear. Nonetheless, modest gains in 1979 sales and earnings are predicted.

Canadian Building Products

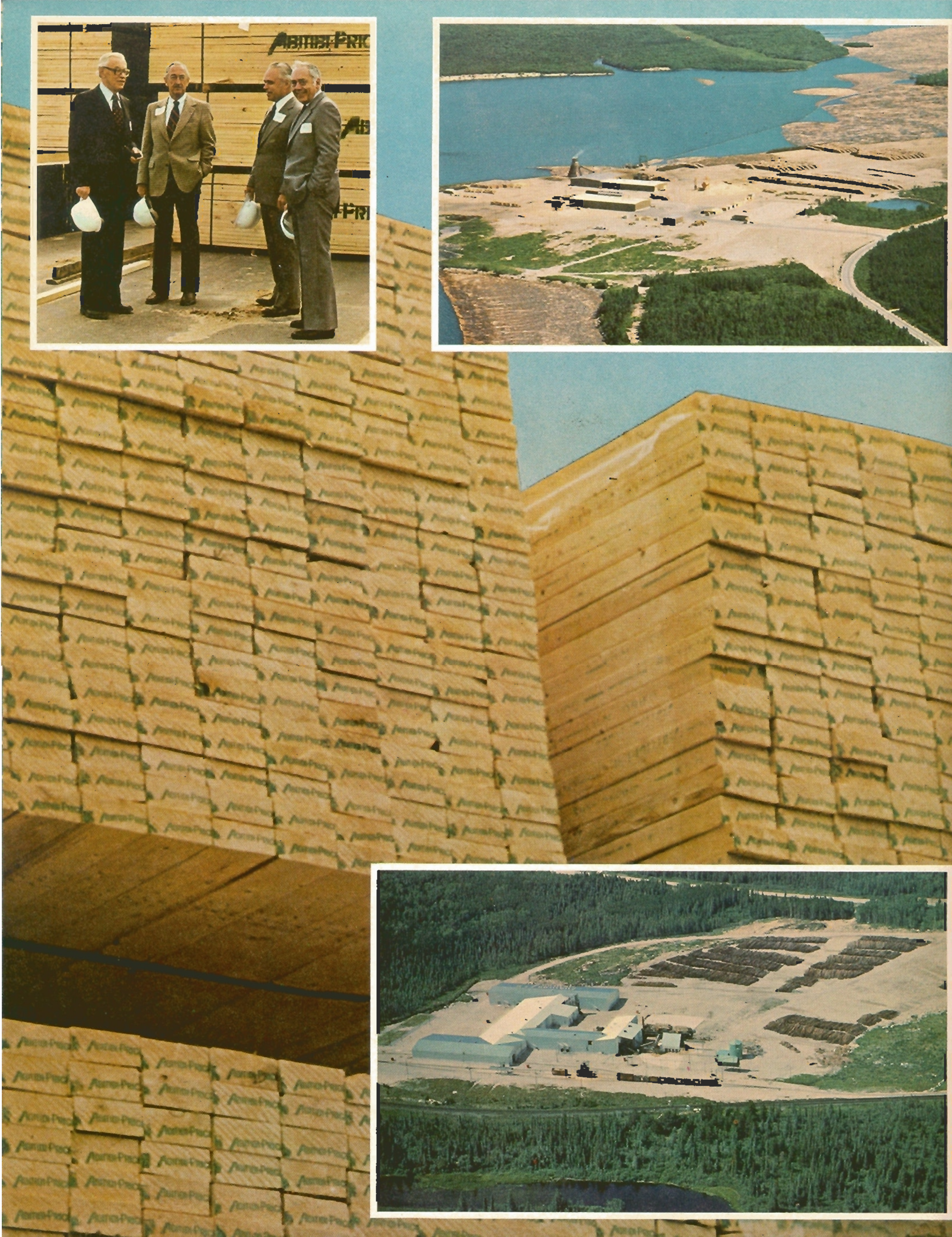
Several factors contributed to a sharp increase in 1978 earnings from the hardboard siding operation at Sturgeon Falls, Ontario. As a result of the combined efforts of research, development and production there was a decided improvement in product quality with minimal cost increases. Additionally, sales increased substantially due to effective sales support and the successful introduction of pre-finished siding into the U.S. market. Looking to 1979, the division expects further growth in sales and earnings.

Packaging

Canadian demand for corrugated containers showed signs of strength only in the second half. Increased corrugating medium demand preceded that of containers and resulted in a substantial increase in sales from Sturgeon Falls. On the other hand, we need to generate sales of considerably more narrow rolls as a

Environmental Control

Expenditures by Abitibi in controlling and treating the liquid waste effluent from its mills has amounted to nearly $60 million since 1960. Shown are some treatment systems for suspended solids used at our mills that include sedimentation lagoons, clarifiers and aerators. Planned expenditure in 1979 is nearly $22 million.



consequence of a change in customer specifications resulted in a drop in earnings from 1977 levels. A capital project, completed early in 1979, permits the "welding" of these narrow rolls into the wider product required by the market, and thereby the recovery of profitability on the associated sales volumes.

Container market conditions led to keen competition which resulted in prices remaining static rather than improving to cover cost increases. Earnings were therefore reduced compared to 1977.

Slight increases in demand for packaging will be coupled with further productivity and modernization measures at Sturgeon Falls, and the Rexdale and Pembroke container plants, to result in some improvement in 1979 sales and earnings.

Paperboard, Kraft Papers and Pulp

Paperboard, kraft paper and bleached kraft pulp are the products of this group, all of which recorded disappointing results in 1978 in spite of near-full operation ratios.

Abitibi is a net buyer of kraft pulp, but the bleached kraft pulp shipments from the Smooth Rock Falls, Ontario mill to other mills within the company as well as the portion delivered to the open market, suffered alike in 1978 from severely depressed prices. These were brought about by world-wide over-capacity and unprecedented producer inventory levels. As a result operating losses were incurred. Over the course of 1978 demand gradually improved, inventories returned to more normal levels and prices began to strengthen. Prices will continue to improve in 1979, and operations will return to a profitable level.

Paperboard and kraft paper felt the effect of stiff competition in their segment of the packaging market where supply continued to outstrip marginally increased demand although the company's operations ran close to capacity. Needed adjustments to prices were not universally applied throughout the industry therefore the company's cost increases were not fully recovered, and paperboard and kraft paper operated at only a small profit.

1978 saw the completion of several major capital programs pointed toward productivity and efficiency in the Jonquière paperboard mill, the cost effectiveness of which will influence favourably the earnings potential of 1979. A continuing but moderate increase is forecast in demand which will enhance industry operating rates, and create an environment for firming prices and improved profitability.

Lumber

Donald C. Parker

Faced with a confusing array of investment alternatives in 1978, the typical U.S. family appears to have settled on home ownership as a reliable inflation hedge, for housing starts there were approximately two million for the second consecutive year—an unusual occurrence in a nearly four-year-old U.S. economic growth phase. The Canadian picture saw a continuation of the downward trend from 278,000 starts in 1976 to 246,000 in 1977 and 223,000 in 1978. Thus the U.S. new housing market and increased activity in re-modelling and repair in both Canada and the U.S. combined to sustain a buoyant lumber market during the year. While prices were steady and relatively high in 1978, they were not at levels such as to permit recovery of relentless cost increases incurred since 1973-74, following which period prices were depressed in response to diminished demand. Nevertheless, and with one exception, all sawmills in the Lumber group, especially those at Terrace, British Columbia, Thunder Bay, Ontario and L'Ascension, Quebec, made substantial contributions to 1978 earnings, a significant turn around from 1977.

The one exception was the new sawmill at White River, Ontario which, after its first full year of operation, had not totally resolved its equipment and personnel difficulties with the result that production goals were not achieved. The remaining problems have been clearly identified and it is expected that their solution in 1979 will mean a positive contribution to earnings.

For 1979, housing starts in the U.S. are expected to decline to about 1.7 million and to remain at about 220,000 in Canada. However, the shortfall in lumber consumption caused by this drop in housing starts will be appreciably compensated for by a continuation of the re-modelling and repair trend, an emphasis on treated lumber for newly-emerging uses in the construction of house foundations and as a substitute for cedar in outdoor applications, and productivity improvements at the sawmills. As a result earnings in 1979 should approach those realized in 1978.

Lumber

Abitibi-Price is the largest producer of lumber in Eastern Canada. Output to the North American market is from seven Canadian sawmills, two of the more recent additions are pictured here. Four Abitibi-Price executives on a visit to the Peribonca mill (L-R) A. A. Labrèque (Price), T. J. Bell, C. R. Tittemore and R. C. Gimlin.

Mineral Interests

The Mattabi base metal mine near Ignace, Ontario a 40%-60% joint venture of Abitibi and Mattagami Lake Mines, milled 960,857 tons of ore grading 6.49% zinc, 0.83% copper 0.67% lead and 2.72 oz. silver per ton in 1978. Earnings rose in the second half reflecting the recovery of base metal prices from their cyclical lows of the first half, and Abitibi's equity in these earnings was $3.3 million and dividends of $4.8 million were received which were below 1977.

The Buchans mine in Newfoundland milled 202,000 tons of ore and produced 30,493 tons of zinc concentrates, 18,300 tons of lead concentrates and 4,890 tons of copper concentrates with associated silver and gold values. After 50 years of continuous production, planning has taken place against the fact that the Buchans Unit ore reserves will be exhausted and mining operations will cease by 1980. During 1978 the tailings ponds were sampled and an encouraging study is under way into the potential for installing a process for the recovery of barite. The Town of Buchans has been incorporated as a Local Development District, most of the inhabitants now own their homes, and the hospital, arena, library and municipal services have all been turned over to the town by the mine.

Exploration continues on Abitibi's holdings of 1,017 square miles of mineral lands in Ontario and drilling has begun on some targets found during exploration programs of the past two years. Also, exploration is in progress in two other areas in Ontario by Abitibi in joint venture with Mattagami Lake Mines. Intensive exploration has also continued on the company's 2,200 square mile mineral rights grant in Newfoundland in search for a mine to replace Buchans, as well as to develop its other mineral showings. Exploration teams were also active in Quebec and New Brunswick.

Capital and Environmental Programs


T. Newman McLenaghen

The 1978 cycle of strategic planning by all the company's business units produced a $700 million capital program for the five years beginning 1979 for which year some $130 million have been allocated. The program is dedicated to the modernization of operations including some incremental capacity increases, improving productivity and costs, upgrading product mix, and improving quality, all with a view to preparing the company for the competitive environment of the challenging years ahead.

The scope and magnitude of the program are substantially greater than has ever been undertaken in the history of Abitibi or Price, and its urgency pointed to the need for specialized management. As a result T.N. McLenaghen was appointed Senior Vice-President with responsibility for engineering, construction, cost control and general administration of all capital projects within the company.

Mr. McLenaghen also carries the responsibility for the company's continuing program of environmental improvement at the mills. In 1978 a number of major environmental projects were completed and a concerted effort was expended to complete studies and set up defined programs to meet the regulations and guidelines of the various Federal, Provincial and State regulatory agencies. In some jurisdictions, such as Quebec, regulations are not yet in place, while Federal standards are under review.

Notable among the accomplishments of 1978 was the closing of the Abitibi-Provincial sulphite mill at Thunder Bay, conversion to sulphur-free pulping at Sturgeon Falls and the installation of a sand settler, clarifier and sludge thickener at Beaupré. Additionally, major programs were completed at Smooth Rock Falls, the newsprint mills in Thunder Bay, and at Alma and Jonquière. In addition to continuing projects at these locations, substantial undertakings will begin at Chandler and Grand Falls in 1979, and the capital program at Kénogami has significant positive environmental implications.

Research and Development

Robert D. Duncan

New processes for chemimechanical pulps and improved mechanical pulps continue to be highlights of the R&D program. Among the advantages offered by these new processes are a major reduction in pollution from newsprint operations as the sulphite pulping component is reduced or possibly eliminated with their use, higher pulp yield per ton of wood, and increased utilization of sawmill residues. These processes have the disadvantage of being energy intensive. In particular, development work continues on the application of chemimechanical pulp to groundwood paper manufacturing at Kenogami, where a plant to produce this type of pulp is now under construction. This plant will replace an obsolete groundwood mill with an ultra-modern pulping process to supplant a mixture of stone groundwood and sulphite pulps. Also, development efforts are directed to further apply this new technology to replace older pulping processes which are no longer compatible with current objectives for a clean environment. Much of the work is at production scale and includes paper machine and pressroom trials.

Paper making R&D activities centre on using advanced electronic measurement techniques to better troubleshoot and understand variations in paper machine operation. By applying this new technology, our engineers and scientists are helping to make more and better products from our mills. Also, key elements of the paper research program are devoted to developing technical data needed for implementation of the company's intensive five year capital program.

As part of its system approach to newsprint research, Abitibi's Research Centre at Sheridan Park, near Toronto has further expanded its capability for printing and printability studies of the new processes that have developed in the past few years. The expanded program is receiving customer support through increased co-operation in pressroom trials and troubleshooting.

Developments in the fine paper area have resulted in new products and marked improvements in many of the traditional products, in line with the long range plans of that segment of the company's business.

Paneiboard and Building Materials R&D continues its quest for new and better products. Particular emphasis is being placed on basic fibre and board properties to achieve improved weatherability, ease of application and appearance.

Personnel

The primary mill union agreements in Ontario, Quebec, Newfoundland and Manitoba were renewed for two years to April 30, 1980, with the settlement falling within the industry pattern. A memorandum of agreement was reached in December following woodlands negotiations in Ontario and Quebec. It was gratifying to conclude these major negotiations with no disruption of operations.

Top priority for accident prevention was ongoing in 1978. The increased emphasis on safety at all levels of the organization contributed to a significant decrease in disabling injuries and an improvement over 1977. With few exceptions, mill safety performances were better than industry averages. 1979 will see vigorous activity in the pursuit of Abitibi's goal to be the industry leader in this most important aspect of human relations.

A number of initiatives were taken during the year to further improve communications and problem-solving effectiveness at all levels of supervision. The Management by Objectives program has been fortified with tutorial seminars, which also addressed means and skills for dialogue between supervisor and supervised.

Moreover, a large number of employees availed themselves of the company's Educational Assistance Plan thereby increasing their knowledge and skills on their own time in order to prepare themselves for career advancement and to enhance their effectiveness in their current positions.

For most of the year, employee compensation was regulated by the Anti-Inflation Board legislation, with which the company complied both as to the letter and spirit.

Throughout the year, employees continued to take an active part in the communities in which they live. Many hold responsible positions on municipal and educational boards and councils, while others provided leadership and assistance through numerous voluntary charitable and business organizations. These activities enabled the company to fulfil part of its social responsibility to the communities in which it is a corporate citizen.

Abitibi and Price Products, Plants and Sales Offices

Products	Manufactured At	Sales Companies and Offices
Newsprint	Pine Falls, Man.; Thunder Bay (2 mills) and Iroquois Falls, Ont.; Beaupré, Alma and Chandler, Que.; Grand Falls, Nfld.; Augusta, Ga.; DeRidder, La.	*Abitibi-Price Sales Corporation New York, N.Y.; Des Plaines, Ill.; Atlanta, Ga.; Troy, Mich.
Uncoated Groundwood Papers	Sault Ste. Marie, Ont.; Jonquière, Que.	*Abitibi-Price Sales Ltd. Toronto, Ont.; Montreal, Que. *Abitibi-Price Sales Company Limited London, England *Each of these companies sells both newsprint and uncoated groundwood paper.
Fine, Printing, Packaging and Business Papers, Wall Paper and Specialty Papers	Thorold, Thunder Bay and Georgetown, Ont.	Abitibi Provincial Paper Toronto, Ont. Montreal, Que.
School, Home and Office Supplies	Toronto, Ont.; Vancouver, B.C.; Joliette, Que.	Hilroy Ltd. Toronto, Ont.; Montreal, Que.; Vancouver, B.C.
Envelopes	Stellarton, N.S.; Montreal, Que.; Toronto, Ont.; Winnipeg, Man.; Calgary, Alta.; Vancouver, B.C.	Canada Envelope Company Stellarton and Halifax, N.S.; Montreal, Que.; Toronto, Ottawa and London, Ont.; Winnipeg, Man.; Calgary and Edmonton, Alta.; Vancouver, B.C.
Wholesale Distribution Fine Paper Products		Inter City Papers Limited Ottawa, Mississauga and London, Ont.; Halifax, N.S. Lauzier, Little Inc. Montreal and Quebec City, Que.
Grocery Bags, Sacks, Paper Towels and Folding Cartons	Lachute, Que.	Price Wilson Major centres across Canada
Building Products and Packaging U.S.A. Hardboard, Woodgrain Hardboard Decorative Hardboard Prefinished Plywood Panels Hardboard Siding Prefinished Mouldings Insulating Sheathing	Alpena, Mich.; Chicago, Ill.; Rancho Cucamonga, Calif.; Roaring River, N.C.; Middlebury, Ind.; Blountstown, Fla.	**Abitibi Corporation Building Products Division Marietta, Ga.; Arlington, Tex.; Troy, Mich.; Barrington, Ill.; Devon, Pa.; Hudson, Ohio; Memphis, Tenn.; Shawnee Mission, Kans.; Middlebury, Ind.; Avon, Conn.; Boundbrook, N.J. **All building products are sold [illegible] the above locations.
Canada Hardboard Siding and Corrugating Medium	Sturgeon Falls, Ont.	Rexdale, Ont.
Corrugated Containers	Rexdale and Pembroke, Ont.	Abitibi Containers Rexdale and Pembroke, Ont.; Montreal, Que.
Paperboard and Kraft Paper	Jonquière, Que.	Price Kraft and Paperboard Corporation Montreal, Que.; Don Mills, Ont.
Kraft Pulp	Smooth Rock Falls, Ont.	Abitibi Paper Company Ltd. Toronto, Ont.
Lumber	Terrace, B.C.; Thunder Bay, Smooth Rock Falls and White River, Ont.; Falardeau, L'Ascension and Price, Que.	Abitibi-Price Lumber Ltd. Toronto and Thunder Bay, Ont.; Vancouver, B.C.
Ties, Treated Wood Products and Treating Services	Thunder Bay, Ont.	Thunder Bay, Ont.

Sales Companies' Principal Officers

Bernd K. Koken, Chairman and Chief Executive Officer
George R. Arellano, President, International and Commercial Division
Laurence E. Mansfield Jr., President, Publisher Division

John G. Hayden, Vice-President, Commercial Sales
R. Blake Moore, Vice-President, Publisher Sales
Ronald E. Blair, Managing Director

Thomas H. Birchall, President

James E. Patterson, President

Robert M. Sleeth, President

Ronald Oberlander, President

Charles F. Buckland, President

Peter P. Armstrong, General Manager
S. Frank Rook, Vice-President and General Manager

Durward B. Geffken, President

Donald C. Parker, President and General Manager

Directors and Officers

Directors

Marcel Bélanger, O.C.
President
Gagnon et Bélanger Inc
Quebec City, Canada

Thomas J. Bell, M.C.
Chairman of the Board
and Chief Executive Officer
Abitibi Paper Company Ltd
Toronto, Canada

Howard W. Blauvelt
Chairman and Chief Executive Officer
Continental Oil Company
Stamford, Connecticut, U.S.A.

Edmund C. Bovey, C.M.
Chairman
Norcen Energy Resources Limited
Toronto, Canada

Marsh A. Cooper
President and Managing Director
Falconbridge Nickel Mines Limited
Toronto, Canada

Robert C. Gimlin
President
and Chief Operating Officer
Abitibi Paper Company Ltd
Toronto, Canada

Leonard G. Lumbers
Chairman of the Board
Noranda Manufacturing Ltd
Toronto, Canada

C. Edward Medland
President and Chief Executive Officer
Wood Gundy Limited
Toronto, Canada

General Lauris Norstad, D.S.M., Silver Star, C.B.E.
Honorary Chairman
Owens-Corning Fiberglas Corporation
Toledo, Ohio, U.S.A.

The Honorable John P. Robarts, P.C., C.C., Q.C.
Partner
Stikeman, Elliott, Robarts & Bowman
Toronto, Canada

C. Harry Rosier
Vice-Chairman of the Board
Abitibi Paper Company Ltd
Toronto, Canada

Kenneth R. Thomson
Chairman of the Board and President
Thomson Newspapers Limited
Toronto, Canada

Charles R. Tittemore
President and Chief Executive Officer
The Price Company Limited
Quebec City, Canada

John A. Tory, Q.C.
President
The Thomson Corporation Limited
Toronto, Canada

William O. Twaits, C.C.
Director
Toronto, Canada

Honorary Director

Harry J. Carmichael

Officers

Thomas J. Bell
Chairman of the Board
and Chief Executive Officer

C. Harry Rosier
Vice-Chairman of the Board

Robert C. Gimlin
President and Chief Operating Officer

Charles R. Tittemore
Group Vice-President

T. Newman McLenaghen
Senior Vice-President

Thomas H. Birchall
Vice-President, Fine Papers

Edward J. Brady
Vice-President, Industrial Relations

Charles F. Buckland
Vice-President,
Building Products and Packaging

John G. Davis
Vice-President,
Fine Paper Group

Robert D. Duncan
Vice-President, Corporate Services

William W. Hall
Vice-President, Corporate Development

William J. Johnston
Vice-President, Woodlands Operations

Mark D. S. Kellow
Vice-President, Personnel

Bruce W. Little
Vice-President,
Newsprint Manufacturing, Region 2

K. Linn Macdonald
Vice-President, Newsprint

J. Ian McGibbon
Vice-President, Finance

Frank L. Morton
Vice-President, Engineering Services

Eugene L. Neal
Vice-President, Public Relations

James B. Papoe
Vice-President,
Newsprint Manufacturing, Region 1

Donald C. Parker
Vice-President, Lumber and Kraft Products

Michael D. Thompson
Secretary and General Counsel

H. Paul Armstrong
Treasurer

Roy Curtis
Assistant Vice-President, Finance

J. Kenneth Stevens
Operations Controller

H. Colin Warner
Corporate Controller

Douglas J. Butler
Assistant Secretary

Robert A. Cook
Assistant Treasurer

Transfer Agents and Registrars

Montreal Trust Company
Toronto, Montreal, Vancouver, Calgary,
Regina, Winnipeg and Halifax, Canada

Citibank N.A.
New York, U.S.A.

Auditors

Price Waterhouse & Co.
Toronto, Canada

Lithographed in Canada
Cover: Kromekote* Cover CC1S 10 pt
Text: Abitibi Provincial's 160M
Kelmscott Smooth

*Kromekote is a registered trademark owned
by Champion International Corporation

ABITIBI PAPER COMPANY LTD.
Head Office Toronto-Dominion Centre.
Toronto, Canada M5K 1B3