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## **FIRST QUARTER INTERIM REPORT**

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**FOR THE THREE MONTHS ENDED MARCH 31, 2002**

**TimberWest Forest Corp.**

## TIMBERWEST FOREST CORP.

### To Our Unitholders,

I am pleased to report that the Company generated distributable cash of \$21.2 million, or \$0.30 per weighted average Stapled Unit for the first quarter of 2002, compared to distributable cash of \$25.9 million, or \$0.40 per weighted average Stapled Unit for the same period in 2001. While these results were better than expected, they were clearly worse than those typically delivered by TimberWest at the start of a new year. Despite all of the difficulties, we were pleased to generate sufficient distributable cash to fund our quarterly distribution at a time when revenues and earnings were down 20% and 25%, respectively, from the first quarter of the prior year.

A broken stumpage and regulatory system on the BC coast, the ongoing softwood lumber dispute with the US, continued weakness in the Japanese economy, and depressed pulp and paper markets made for very difficult conditions in the first quarter of 2002. More than half of the BC coastal logging and sawmilling industry was not operating during this past quarter. While private land logging operations functioned, most public land logging, including the operations of TimberWest, were down for the quarter and they continue to be down. As a result, volumes and prices for all of TimberWest's products (logs, lumber and chips) were lower than those for the same period in the prior year.

Domestic log sales volumes for the quarter were down 44% over the equivalent period in 2001. This reflects the structural issues the BC coast is facing and the negative impact on our domestic log customers created by continued uncertainty surrounding trade talks with the US and the decision to impose duties on softwood lumber exports, including cedar. This uncertainty also means that our Elk Falls lumbermill continues to be unable to access the US market profitably.

Fortunately, the decline in domestic sales was almost completely offset by higher export log sales, a result made possible by the private ownership of TimberWest's forest lands. Log exports are a critical part of our success because, like any business, we want to diversify our markets and get the highest value for our product. The premium received by selling a small portion of our logs for international prices allows TimberWest to harvest stands that would otherwise be uneconomic. This is what has enabled us to continue operating profitably on private land and to keep employees working at a time when most Crown timber-dependent companies are severely curtailed.

As I reported to you last quarter, TimberWest has a new strategic plan in place to enhance our strengths through achieving operations excellence. A big part of this is cost reduction. During the first quarter we identified, evaluated and initiated many cost-saving projects, with the expectation that many of the benefits will only begin to materialize as we progress through the year and after we incur some "start-up" costs to initiate the required changes. Costs were in fact lower in the first quarter. While some of this is due to the fact that we're harvesting at lower elevations and have had to shut down production at some of our higher cost operations on Crown land, we have also made a good start on permanent cost reduction by taking out \$1.9 million in costs in the quarter towards our 2002 target. Our new Vice-President of Operations, John Mann, has been on board for only two months and I am pleased with his progress on this and many other initiatives.

On our public timberlands operation, we are working with all stakeholders – licensees, the IWA, the Truck Loggers Association and the provincial government – to find solutions and create a viable industry on the coast. It is a complicated process and, while it is taking some time to find solutions, I am confident we will see legislative changes that will enhance the competitiveness of the coastal BC industry.

It has been a difficult quarter and TimberWest employees have risen to the challenge, not just in terms of production, but by staying focused on safety. The Company has set an aggressive MIR safety target of 6 for 2002, and in the first quarter has achieved an MIR of 3.86.

As the fiscal year progresses, TimberWest will continue to do all it can internally to improve our profitability by reducing costs and enhancing efficiencies.

Thank you for your support.

On behalf of the Board of Directors





**TIMBERWEST FOREST CORP.**

Paul J. McElligott  
President and Chief Executive Officer

Vancouver, British Columbia  
April 11, 2002



# TIMBERWEST FOREST CORP.

## Management's Discussion and Analysis

For the three months ended March 31, 2002

*Management's Discussion and Analysis supplements, but does not form part of, the unaudited interim consolidated financial statements of TimberWest Forest Corp. ("TimberWest") and the notes thereto for the first quarter of 2002. This discussion and analysis provides an overview of significant developments that have affected TimberWest's performance during the first quarter of 2002 relative to the first quarter of 2001, and that have affected the Company's financial position as at March 31, 2002 relative to December 31, 2001. Factors that could affect future operations are also discussed. These factors may be affected by known and unknown risks and uncertainties that may cause the actual future results of the Company to be materially different than those expressed or implied in this discussion. These risks and uncertainties are described herein and in the Management's Discussion and Analysis contained in the Company's 2001 Annual Report.*

### Quarterly Financial Highlights

TimberWest generated distributable cash<sup>1</sup> of \$21.2 million, or basic and diluted distributable cash of \$0.30 per weighted average Stapled Unit for the quarter ended March 31, 2002, compared to distributable cash of \$25.9 million, or basic and diluted distributable cash of \$0.40 per weighted average Stapled Unit for the same period in 2001. Earnings available for distribution<sup>1</sup> for the quarter, before provision for future income taxes, were \$14.9 million or \$0.21 per weighted average Stapled Unit compared to \$21.3 million, or \$0.33 per weighted average Stapled Unit for the same quarter in 2001. Net sales for the first quarter were \$88.9 million, compared to net sales of \$110.7 million reported for the first quarter of 2001. Operating earnings were \$21.0 million for the first quarter of 2002 compared to \$28.0 million for the same quarter in 2001. EBITDA<sup>1</sup> for the quarter ended March 31, 2002 was \$23.7 million, or \$0.34 per weighted average Stapled Unit compared to \$31.6 million, or \$0.49 per weighted average Stapled Unit for the same period in 2001.

In February 2002, the Company completed an equity offering through a syndicate of underwriters of 11,190,650 Stapled Units at a price of \$12.85 per Stapled Unit, for gross proceeds of \$143.8 million. Net proceeds of the offering of \$136.1 million were used to reduce the Company's indebtedness under its non-revolving credit facility.

### Cash Distributions

On April 11, 2002, TimberWest announced a distribution of \$0.269 per Stapled Unit, payable July 15, 2002 to Unitholders of record on July 1, 2002. Due to the seasonal and cyclical nature of TimberWest's business, cash flows may fluctuate from quarter to quarter and from year to year. One of the objectives of TimberWest's cash distribution policy is to make even distributions to unitholders, which may differ from actual cash generated during the period.

### Operating Highlights

Log sales for the three months ended March 31, 2002, were \$73.0 million, down 10% from log sales of \$81.1 million for the quarter ended March 31, 2001. This overall decrease in log sales can be partially attributed to a 3% decrease in log sales volumes over the comparative period in 2001, with log shipments for the three months ended March 31, 2002 amounting to 649.8 thousand m<sup>3</sup> compared to 667.2 thousand m<sup>3</sup> for the first quarter of 2001. Despite adverse conditions in all markets, the Company was able to increase sales volumes into its export markets by 98% compared to export sales in the first quarter of 2001, offsetting a 44% decrease in domestic sales volume over the comparative period in 2001. A decrease in average realizations on log sales to \$112 per m<sup>3</sup> for the first quarter of 2002, from \$122 per m<sup>3</sup> for the comparative quarter in 2001, further contributed to the overall decline in log sales compared to the prior year.

The impacts of lower log sales volumes and log sales realizations in the first quarter of 2002 relative to the comparative period of 2001 were partially mitigated by an improvement in TimberWest's logging cost of sales. Unit logging cost of sales were down to \$71 per m<sup>3</sup> from \$77 per m<sup>3</sup> for the comparative quarter in 2001, a decrease

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<sup>1</sup> Distributable cash, earnings available for distribution and EBITDA are measures that do not have a standardized meaning prescribed by Canadian generally accepted accounting principles ("GAAP") and may not be comparable to similar measures presented by other companies. A reconciliation between net earnings as determined in accordance with GAAP and distributable cash and earnings available for distribution is provided in the Consolidated Statements of Distributable Cash included in this interim report. A reconciliation between net earnings as determined in accordance with GAAP and EBITDA is provided in the supplemental information appended to this interim report.



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attributable to reduced production on the Company's higher-cost Crown tenures and to a combination of reduced road building activity, harvesting at lower elevations due to snow-pack at higher levels and a reduction in the average cost of log purchases due to low market prices. In addition, cost reduction initiatives for the quarter have yielded \$1.9 million towards the 2002 target.

Lumber sales were \$12.7 million for the quarter ended March 31, 2002, down from \$22.1 million for the same period in 2001. The 2001 figures include the sale of products from the Cowichan Lumbermill which was closed in early 2001. For Elk Falls, 2002 year-to-date sales of \$12.7 million are down slightly from \$13.8 million reported for the three months ended March 31, 2001. Overall weakness in all markets for the Company's lumber products resulted in a 7% decrease in Elk Falls' sales volumes, as well as a 1% decrease in sales realizations over the comparative period in the prior year.

Overall weakness in the forest products sector, combined with chip production solely from Elk Falls in 2002, contributed to a decrease in wood chip sales volumes and realizations during the first quarter of 2002 compared to the comparative period in 2001. In addition, there were fewer real estate transactions in the quarter compared to the first quarter of 2001. Both of these factors had an unfavorable impact on first quarter operating earnings for 2002.

### Financial Position

Working capital, excluding the Company's credit facilities and the distribution payable, increased by \$2.7 million during the quarter ended March 31, 2002, to \$53.1 million. This increase can be attributed to a slight increase in inventories and prepaid expenses as well as a decrease in accounts payable and accrued liabilities, offset by a decrease in accounts receivable.

Included in current liabilities at March 31, 2002, is \$63.0 million drawn on the non-revolving credit facility which matures on December 31, 2002, and \$125.0 million for debentures which mature on March 3, 2003. On their maturity, the Company anticipates refinancing both of these liabilities through the debt markets.

The distribution payable at March 31, 2002, of \$20.4 million is \$3.0 million greater than the distribution payable at December 31, 2001, and reflects the increased number of Stapled Units outstanding as a result of the equity offering completed during the quarter.

As at March 31, 2002, TimberWest's consolidated debt was \$241.0 million compared to a balance of \$378.6 million as at December 31, 2001. The Company's consolidated debt-to-equity ratio as at March 31, 2002 was 21:79, an improvement over the ratio of 32:68 as at December 31, 2001. These favorable results can be attributed to the issuance of 11,190,650 Stapled Units in February 2002 on the completion of the equity offering during the quarter and the use of the net proceeds from the offering of \$136.1 million to pay down the Company's non-revolving credit facility. The payment on the non-revolving facility resulted in a reduction in funds available to the Company through this facility, from \$200.0 million to \$63.0 million. Total debt facilities available to the Company as at March 31, 2002 were \$323.0 million.

During the quarter ended March 31, 2002, options to purchase 64,251 Stapled Units were exercised for proceeds of \$0.6 million and options to purchase 15,000 Stapled Units were granted.

### Cash Flow and Liquidity

Net cash generated from operations, before changes in non-cash working capital, for the three months ended March 31, 2002, was \$21.2 million or \$0.30 per weighted average Stapled Unit compared to \$24.1 million or \$0.37 per weighted average Stapled Unit for the corresponding quarter in 2001. Non-cash working capital increased by \$2.7 million during the first quarter of 2002 compared to a \$13.2 million increase during the same period in 2001. These increases primarily reflect an increase in inventory and prepaid expense balances to seasonal levels.

Net cash used for financing activities during the first quarter of 2002 was \$18.3 million, an increase of \$5.8 million over the same quarter in 2001. As noted previously, a bought deal public offering closed during the first quarter of 2002, concluding with the issuance of 11,190,650 Stapled Units for net proceeds of \$136.1 million. The proceeds from the bought deal were used to repay amounts borrowed on the Company's non-revolving credit facility. The first quarter distribution of \$0.269 per Stapled Unit paid to unitholders in January 2002 was the same as that paid in January of the prior year, however, the total amount paid was lower as there were slightly less Stapled Units



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outstanding at the beginning of the first quarter of 2002 compared to the first quarter of 2001. During the first quarter of 2002, the Company received \$0.6 million for Stapled Units issued on the exercise of 64,251 Stapled Unit options.

Net cash used in investing activities was \$0.2 million in the first quarter of 2002, compared to net cash provided by investing activities of \$1.6 million for the same quarter of 2001. The variance from the prior year can largely be attributed to sales of capital assets and real estate properties being lower than the prior year, coming in at \$0.8 million versus \$3.6 million for the first quarter of 2001. Capital expenditures of \$0.3 million for the quarter ended March 31, 2002, were comparable to those for the corresponding period in 2001. Other assets increased by \$0.7 million during the first quarter of 2002, less than the increase of \$1.6 million for the first quarter of 2001, primarily due to a rebate of Workers Compensation Board premiums included in the 2001 amount.



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## Accounting Policy Change

Effective January 1, 2002, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3870 – *Stock-based Compensation and Other Stock-based Payments*. The new recommendations establish standards for the recognition, measurement, and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services provided by employees and non-employees. Section 3870 sets out a fair value based method of accounting that is required for certain, but not all, stock-based transactions. The new standard permits the Company to continue its existing policy that no compensation cost is recorded on the grant of Stapled Unit options to employees. Consideration paid by employees on the exercise of Stapled Unit options is recorded as share capital. However, Section 3870 requires additional disclosures for options granted to employees, including disclosure of pro forma earnings and pro forma earnings per share as if the fair value based accounting method had been used to account for employee stock options.

## Normal Course Issuer Bid

Pursuant to a normal course issuer bid, TimberWest may repurchase, in the open market through the facilities of the Toronto Stock Exchange, up to 3,252,350 Stapled Units, representing approximately 5% of the Company's issued and outstanding Stapled Units as of the date of acceptance of the bid, in the 12 months commencing October 29, 2001. As at March 31, 2002 TimberWest has not repurchased any of its Stapled Units through this instrument.

## Outlook

Considerable uncertainty remains in the US lumber market. The Canada – US Softwood Lumber dispute has yet to be resolved. The International Trade Commission's final determination of injury to the US industry, expected in mid May, will bring some clarity to North American lumber markets. The final imposition of countervailing and anti-dumping duties should provide price support in both lumber and log markets. Improving economic conditions should lead to higher lumber consumption in areas other than new home construction. New home construction is expected to continue to show the strength that it has exhibited in recent years.

Economic reports indicate that the Japanese economy is not expected to change significantly during 2002. In particular, housing starts are expected to remain consistent with 2001 at 1.2 million. As a consequence, the Japanese lumber market should remain stable for the balance of the year, with the Company anticipating both log and lumber pricing and demand to remain stable.

To date, there has been little good news in global pulp markets, and economic forecasts suggest no improvement will occur during the balance of 2002. Locally, pulp log prices in the coastal British Columbia market remain weak, but stable, with no improvement expected for the balance of the year.

TimberWest continues to work with industry stakeholders on public policy reform and cost reduction initiatives with a view to improving the competitiveness of the forest industry on the coast. The Company is hopeful that meaningful change will occur this year to improve industry viability. Concurrently, TimberWest will be working on its own set of cost reduction initiatives throughout the remainder of the year.

Despite the fact that market conditions are not expected to improve appreciably in the near term, TimberWest will continue to focus on its strategy of operations excellence to drive costs down throughout the business, and to use the flexibility of its asset base and its market diversity to deliver consistent results to Unitholders.

*The statements which are not historical facts contained in this report are forward-looking statements that involve risks and uncertainties. TimberWest's actual results could differ materially from those expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, general economic conditions, variations in TimberWest's product prices and changes in commodity prices generally, changes in market conditions, actions of competitors, interest rate and foreign currency fluctuations, regulatory and harvesting*

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*fee changes and other actions by governmental authorities, the ability to implement business strategies and pursue business opportunities, weather conditions, forest fires and other natural phenomena and other risks and uncertainties described in TimberWest's public filings with securities regulatory authorities.*

# TIMBERWEST FOREST CORP.

## Consolidated Statements of Distributable Cash

(in millions of dollars, except per Stapled Unit amounts)  
Unaudited

	For the three months ended March 31, 2002	For the three months ended March 31, 2001
Net earnings	\$ 7.7	\$ 12.2
Income tax benefit related to distributions	6.2	7.8
Earnings available for distribution	13.9	20.0
Future income tax expense	1.0	1.3
Earnings available for distribution before provision for future income tax expense	14.9	21.3
Add (deduct):		
Depreciation, depletion and amortization	4.6	3.8
Proceeds from sale of capital assets	0.8	3.6
Gain on sale of capital assets	(0.2)	(0.8)
Maintenance capital expenditures	(0.3)	(0.4)
Other non-cash items	1.4	(1.6)
	6.3	4.6
<b>Distributable cash</b>	<b>\$ 21.2</b>	<b>\$ 25.9</b>
<b>Basic and diluted distributable cash per Stapled Unit</b>	<b>\$ 0.30</b>	<b>\$ 0.40</b>
<b>Cash distributions paid per Stapled Unit</b>	<b>\$ 0.27</b>	<b>\$ 0.27</b>
Basic weighted average number of Stapled Units outstanding at the end of the period (000's)	70,388	64,912
Diluted weighted average number of Stapled Units outstanding at the end of the period (000's)	70,588	65,050
Stapled Units outstanding at the end of the period (000's)	75,946	64,975

## Quarterly Comparison of Distributable Cash

Unaudited	2002	2001	2000	1999	1998
<b>Distributable Cash</b> (in millions of dollars)					
First	\$ 21.2	\$ 25.9	\$ 28.4	\$ 24.5	\$ 13.2
Second		26.7	28.2	25.1	24.0
Third		14.1	14.1	14.0	11.5
Fourth		16.8	18.5	19.7	19.6
	\$ 21.2	\$ 83.5	\$ 89.2	\$ 83.3	\$ 68.3
<b>Distributable Cash per Stapled Unit</b> (in dollars)					
First	\$ 0.30	\$ 0.40	\$ 0.41	\$ 0.36	\$ 0.19
Second		0.41	0.42	0.36	0.34
Third		0.22	0.22	0.20	0.17
Fourth		0.26	0.29	0.28	0.28
	\$ 0.30	\$ 1.29	\$ 1.34	\$ 1.20	\$ 0.98

See accompanying notes to unaudited interim consolidated financial statements.

# TIMBERWEST FOREST CORP.


## Consolidated Balance Sheets

(in millions of dollars)

	As at March 31, 2002 <i>Unaudited</i>	As at December 31, 2001
<b>Assets</b>		
Current assets:		
Accounts receivable	\$ 29.1	\$ 32.1
Inventories	55.6	54.2
Prepaid expenses and other current assets	3.5	2.3
Future income taxes	3.0	3.0
	91.2	91.6
Capital assets, net	1,366.2	1,369.1
Other assets	23.2	26.5
	\$ 1,480.6	\$ 1,487.2
<b>Liabilities and Unitholders' Equity</b>		
Current liabilities:		
Overdraft facility	\$ 4.0	\$ 3.6
Accounts payable and accrued liabilities	38.1	41.2
Distribution payable	20.4	17.4
Non-revolving credit facility (note 3)	63.0	200.0
Debentures (note 4)	125.0	-
	250.5	262.2
Revolving credit facility	49.0	50.0
Debentures	-	125.0
Long-term silviculture liability	4.7	4.9
Non-pension post-retirement benefits	22.8	22.7
Future income taxes	232.1	233.9
	559.1	698.7
Unitholders' equity		
Stapled Units, consisting of Series A Subordinate Notes, preferred shares and common shares (note 5)	867.6	728.1
Retained earnings	53.9	60.4
	921.5	788.5
	\$ 1,480.6	\$ 1,487.2

See accompanying notes to unaudited interim consolidated financial statements.

On behalf of the Board of Directors:



Paul J. McElligott  
Director



V. Edward Daughney  
Director

# TIMBERWEST FOREST CORP.

## Consolidated Statements of Cash Flows

(in millions of dollars)  
Unaudited

	For the three months ended March 31, 2002	For the three months ended March 31, 2001
<b>Cash provided by (used in):</b>		
<b>Operating activities:</b>		
Earnings before income taxes	\$ 15.1	\$ 21.6
Cash income taxes (note 6)	(0.2)	(0.3)
	14.9	21.3
Items not involving cash:		
Depreciation, depletion and amortization	4.6	3.8
Gain on sale of capital assets	(0.2)	(0.8)
Other non-cash items	1.9	(0.2)
	21.2	24.1
Changes in non-cash working capital:		
Accounts receivable	3.0	0.7
Inventories	(1.4)	(7.4)
Prepaid expenses and other working capital	(1.2)	(2.9)
Accounts payable and accrued liabilities	(3.1)	(3.6)
	18.5	10.9
<b>Financing activities:</b>		
Issuance of Stapled Units, net	136.1	-
Issuance of Stapled Units on exercise of options	0.6	1.3
Increase in overdraft facility	0.4	-
Decrease in non-revolving credit facility	(137.0)	-
Decrease in revolving credit facility	(1.0)	-
Increase in operating loan	-	3.7
Distributions paid to unitholders	(17.4)	(17.5)
	(18.3)	(12.5)
<b>Investing activities:</b>		
Maintenance capital expenditures	(0.3)	(0.4)
Proceeds from sale of capital assets	0.8	3.6
Increase in other assets	(0.7)	(1.6)
	(0.2)	1.6
<b>Increase in cash</b>	-	-
<b>Cash, beginning of period</b>	-	-
<b>Cash, end of period</b>	\$ -	\$ -
<b>Supplemental information:</b>		
Interest paid	\$ 5.6	\$ 8.1
Income taxes paid	\$ 0.2	\$ 0.3

See accompanying notes to unaudited interim consolidated financial statements.

# TIMBERWEST FOREST CORP.

## Consolidated Statements of Operations

(in millions of dollars)  
Unaudited

	For the three months ended March 31, 2002	For the three months ended March 31, 2001
Net sales	\$ 88.9	\$ 110.7
Operating costs and expenses:		
Cost of products sold	61.3	75.3
Depreciation, depletion and amortization	2.6	3.4
Selling, administrative and other	4.0	4.0
	<b>67.9</b>	<b>82.7</b>
Operating earnings	21.0	28.0
Interest expense	4.0	6.2
Amortization of deferred financing costs	2.0	0.4
Other income	(0.1)	(0.2)
	<b>5.9</b>	<b>6.4</b>
Earnings before income taxes	15.1	21.6
Income tax expense (note 6)	7.4	9.4
Net earnings for the period	\$ 7.7	\$ 12.2
<i>Basic and diluted earnings (loss) per common share (note 7)</i>	<i>\$ (0.09)</i>	<i>\$ 0.04</i>

## Consolidated Statements of Unitholders' Equity

(in millions of dollars)  
Unaudited

	Stapled Units		Retained earnings	Total unitholders' equity
	Number	Amount		
<b>For the three months ended March 31, 2002</b>				
Balance December 31, 2001	64,690,867	\$ 728.1	\$ 60.4	\$ 788.5
Issuance of Stapled Units, net (note 5)	<b>11,190,650</b>	<b>138.9</b>	-	<b>138.9</b>
Issuance of Stapled Units on exercise of options	<b>64,251</b>	<b>0.6</b>	-	<b>0.6</b>
Net earnings	-	-	<b>7.7</b>	<b>7.7</b>
Interest on Series A Subordinate Notes	-	-	<b>(20.4)</b>	<b>(20.4)</b>
Income tax benefit thereon	-	-	<b>6.2</b>	<b>6.2</b>
Balance, March 31, 2002	<b>75,945,768</b>	<b>\$ 867.6</b>	<b>\$ 53.9</b>	<b>\$ 921.5</b>
<b>For the three months ended March 31, 2001</b>				
Balance December 31, 2000	64,825,336	\$ 731.4	\$ 56.3	\$ 787.7
Issuance of Stapled Units on exercise of options	150,000	1.3	-	1.3
Net earnings	-	-	12.2	12.2
Interest on Series A Subordinate Notes	-	-	(17.5)	(17.5)
Income tax benefit thereon	-	-	7.8	7.8
Balance, March 31, 2001	64,975,336	\$ 732.7	\$ 58.8	\$ 791.5

See accompanying notes to unaudited interim consolidated financial statements.



# TIMBERWEST FOREST CORP.

## Notes to Unaudited Interim Consolidated Financial Statements

For the three months ended March 31, 2002

(Financial figures presented in the tables that follow are in millions of dollars, except for amounts per Stapled Unit and components thereof.)

### 1. Significant Accounting Policies

These unaudited interim consolidated financial statements include the accounts of TimberWest Forest Corp. and its subsidiaries. Not all disclosures required by Canadian generally accepted accounting principles for annual financial statements are presented, and accordingly, these interim financial statements should be read in conjunction with the Company's most recent annual consolidated financial statements. These interim financial statements follow the same accounting policies and methods of application used in the Company's audited annual consolidated financial statements of December 31, 2001, except for those standards which have changed subsequent to that date, as detailed below. Certain figures for previous periods have been reclassified to conform with the current period's financial statement presentation.

### 2. Accounting Policy Change

#### *Stock-based Compensation*

Effective January 1, 2002, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3870 – *Stock-based Compensation and Other Stock-based Payments*. The new recommendations establish standards for the recognition, measurement, and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services provided by employees and non-employees. Section 3870 sets out a fair value based method of accounting that is required for certain, but not all, stock-based transactions. Section 3870 must be applied to all stock-based payments to non-employees, and to employee awards that are direct awards of stock that call for settlement in cash or other assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments. This new standard is mandatory for fiscal years beginning on or after January 1, 2002, and is to be given retroactive application for certain awards outstanding at the effective date, and prospective application for new awards granted after the effective date.

However, the new standard permits the Company to continue its existing policy that no compensation cost is recorded on the grant of Stapled Unit options to employees. Consideration paid by employees on the exercise of Stapled Unit options is recorded as share capital. Section 3870, however, does require additional disclosures for options granted to employees, including disclosure of pro forma earnings and pro forma earnings per share as if the fair value based accounting method had been used to account for employee stock options (see note 8).

### 3. Credit Facilities

During the quarter ended March 31, 2002, the Company made a payment of \$137.0 million on its non-revolving credit facility, reducing this liability from \$200.0 million to \$63.0 million. This payment resulted in a direct reduction in funds available to the Company through this facility, from \$200.0 million to \$63.0 million. Total debt facilities available to the Company as at March 31, 2002 were \$323.0 million.

### 4. Debentures

The Company's 6.5% Debentures mature on March 3, 2003 and have therefore been classified with current liabilities at March 31, 2002.

### 5. Stapled Units

In February 2002, the Company completed a bought deal public offering through a syndicate of underwriters of 11,190,650 Stapled Units at a price of \$12.85 per Stapled Unit for gross proceeds of \$143.8 million. Net cash proceeds received were \$136.1 million after costs of \$7.7 million (\$4.9 million after future income tax benefit of \$2.8 million).

# TIMBERWEST FOREST CORP.

## Notes to Unaudited Interim Consolidated Financial Statements

For the three months ended March 31, 2002

### 6. Income Taxes

Income tax expense consists of:

	For the three months ended March 31	
	2002	2001
Current income tax		
Large corporation tax	\$ 0.2	\$ 0.3
Income tax benefit on interest on Series A Subordinate Notes charged directly to distributions	6.2	7.8
	6.4	8.1
Future income tax	1.0	1.3
	\$ 7.4	\$ 9.4

### 7. Earnings Available for Distribution per Stapled Unit and Components Thereof

	For the three months ended March 31	
	2002	2001
<b>Net Earnings</b>		
Net earnings	\$ 7.7	\$ 12.2
Less: Distributions on Series A Subordinate Notes	(20.4)	(17.5)
Tax benefit thereon	6.2	7.8
	(14.2)	(9.7)
Earnings (loss) attributable to common shares	(6.5)	2.5
Earnings available for distribution attributable to Series A Subordinate Notes	20.4	17.5
Earnings available for distribution attributable to Stapled Units	\$ 13.9	\$ 20.0
<b>Weighted Average Number of Stapled Units</b>		
Basic weighted average number of Stapled Units	70,387,910	64,912,003
Incremental Stapled Units from potential exercise of options	200,364	137,822
Diluted weighted average number of Stapled Units	70,588,274	65,049,825
<b>Per Stapled Unit Amounts</b>		
Basic and diluted earnings (loss) per common share	\$ (0.09)	\$ 0.04
Basic and diluted earnings available for distribution per Series A Subordinate Note	0.29	0.27
Basic and diluted earnings available for distribution per Stapled Unit	\$ 0.20	\$ 0.31

The Company may elect to pay the interest on, and the principal amount of, Series A Subordinate Notes in common or preferred shares of the Company.

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# TIMBERWEST FOREST CORP.

## Notes to Unaudited Interim Consolidated Financial Statements

For the three months ended March 31, 2002

### 8. Stock-Based Compensation Plans

Under the Company's Stapled Unit Option Plan established in 2000, the Company may grant options for the purchase of Stapled Units to directors, officers or employees who are in active service or employment of the Company or of any of its subsidiaries. In November 2001, to facilitate the wind-up of the Company's Stapled Unit Incentive Plan, the Company introduced a supplement to the Stapled Unit Option Plan called the Distribution Equivalent Plan. Under this supplemental plan, the Company awards Stapled Unit option holders an amount equal to actual distributions paid on the Company's Stapled Units. Awards granted under the Distribution Equivalent Plan vest under the same terms that apply to the corresponding options and can only be exercised at the time of exercise of the corresponding options.

The Company's policy is that no compensation cost is recorded on stock-based compensation awards granted to employees under the Stapled Unit Option Plan. Consideration paid by employees on the exercise of these options is recorded as an addition to Stapled Units. Accordingly, no compensation cost has been recognized for the Stapled Unit Option Plan. Had the compensation cost for the 15,000 Stapled Unit options issued under the Stapled Unit Option Plan between January 1, 2002 and March 31, 2002 been determined based on their fair value at the grant date of the awards, consistent with the fair value method of accounting for stock-based compensation, there would have been no adjustment to the Company's net income and earnings per common share reported for the three months ended March 31, 2001. The fair value of each option grant was estimated at the grant date using the Black-Scholes option pricing model with the following assumptions: distribution yield of 8.4%; expected volatility of 27%; risk-free interest rate of 5.6%; and expected option life of 5 years.

The Company applies the principles of the fair value based method of accounting for stock-based compensation to awards granted under the Distribution Equivalent Plan. Awards are accrued on a basis equal to actual distributions paid on the Company's issued and outstanding Stapled Units and are charged to income as the underlying Stapled Unit options vest. For the three months ended March 31, 2002, \$0.3 million has been accrued for awards granted under this plan relating to the January 2002 distribution paid to unitholders. Of this amount, \$0.2 million has been amortized against income for the quarter.

During the quarter ended March 31, 2002, a total of 64,251 Stapled Unit options with an exercise price of \$8.91 were exercised. As noted previously, a total of 15,000 Stapled Unit options were granted during the quarter ended March 31, 2002, each with an exercise price of \$12.87 and exercisable until February 3, 2007.

# TIMBERWEST FOREST CORP.

## Supplemental Information

For the three months ended March 31

Unaudited

2002

2001

	2002	2001
<b>Sales by Product</b>		
<i>(in millions of dollars)</i>		
Logs	\$ 73.0	\$ 81.1
Lumber	12.7	22.1
Wood chips and other	2.5	3.9
Real estate	0.7	3.6
	<b>\$ 88.9</b>	<b>\$ 110.7</b>
<b>Sales Volume</b>		
Logs ( <i>thousand m<sup>3</sup></i> )	649.8	667.2
Lumber ( <i>million fbm</i> )	26.8	46.6
<b>Production Volume</b>		
Logs ( <i>thousand m<sup>3</sup></i> )	707.5	873.2
Lumber ( <i>million fbm</i> )	26.0	36.0
<b>Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)*</b>		
<i>(in millions of dollars)</i>		
Earnings before income taxes	\$ 15.1	21.6
Add:		
Interest expense	4.0	6.2
Depreciation, depletion and amortization	2.6	3.4
Amortization of deferred financing costs	2.0	0.4
<b>EBITDA</b>	<b>\$ 23.7</b>	<b>\$ 31.6</b>

\* EBITDA does not have a standardized meaning prescribed by Canadian generally accepted accounting principles and may not be comparable to similar measures presented by other companies.

