

Condensed consolidated interim financial statements of

Conifex Timber Inc.

March 31, 2016
(Unaudited)

Conifex Timber Inc.

Condensed consolidated balance sheet
as at March 31, 2016 (unaudited)

(thousands of Canadian dollars)	Notes	As at March 31, 2016	As at December 31, 2015
		\$	\$
Assets			
<i>Current assets</i>			
Cash		7,371.7	9,902.9
Cash - restricted	7	10,418.8	8,545.7
Trade and other receivables		26,002.2	25,929.4
Prepaid expenses and deposits		11,367.8	11,108.2
Inventories	5	53,439.1	43,231.9
Assets held for sale		10.9	10.9
Current assets		108,610.5	98,729.0
Goodwill		3,310.5	3,310.5
Intangible assets		6,910.3	7,843.1
Property, plant and equipment		216,767.9	220,553.3
Deposits		1,727.6	1,661.7
Total assets		337,326.8	332,097.6
Liabilities			
<i>Current liabilities</i>			
Trade payables, accrued liabilities and other payables		26,252.6	23,799.5
Current portion of reforestation obligations		2,734.6	2,773.9
Employee liabilities		2,030.4	1,791.0
Operating loans	6	23,758.3	18,326.9
Current portion of convertible notes	7	11,850.5	11,797.7
Current portion of mortgage	7	11,244.1	11,957.8
Current portion of long-term debt	7	4,019.1	4,353.3
Current liabilities		81,889.6	74,800.1
Reforestation obligations		7,851.4	6,091.4
Environmental liabilities		1,517.6	1,529.6
Other long-term liabilities		12,923.2	13,089.5
Payment-in-kind note	7	-	30,000.0
Long-term debt	7	98,103.9	100,228.3
Non-current liabilities		120,396.1	150,938.8
Total liabilities		202,285.7	225,738.9
Equity			
Share capital		158,082.6	157,835.6
Conversion option on convertible notes		326.4	326.4
Contributed surplus		11,433.1	11,484.6
Deficit		(34,801.0)	(63,287.9)
Total equity		135,041.1	106,358.7
Total liabilities and equity		337,326.8	332,097.6

Events after the Reporting Period (Note 12)

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Conifex Timber Inc.

Condensed consolidated statement of net income and comprehensive income
period ended March 31, 2016 (unaudited)

(thousands of Canadian dollars)	Notes	3 months ended March 31,	
		2016	2015
		\$	\$
Revenue		99,514.5	85,262.9
Costs and expenses			
Cost of goods sold		78,428.7	67,425.2
Freight and distribution costs		14,321.9	13,011.4
Selling, general and administrative		3,732.1	3,749.0
		96,482.7	84,185.6
Operating income		3,031.8	1,077.3
Gain (loss) on disposal of assets	7(c)	28,968.1	(2.2)
Interest expense and accretion		(2,546.1)	(1,268.1)
Other income (expense)		132.4	(85.3)
Foreign exchange gain (loss)		(1,099.3)	1,885.0
		25,455.1	529.4
Net income and comprehensive income for the period		28,486.9	1,606.7
Net income per common share: (in dollars)			
Basic		1.35	0.08
Diluted		1.24	0.08

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Conifex Timber Inc.

Condensed consolidated statement of changes in equity
period ended March 31, 2016 (unaudited)

(thousands of Canadian dollars)	Share capital	Conversion option on convertible notes	Contributed surplus	Deficit	Total equity
	\$	\$	\$	\$	\$
Balance at December 31, 2014	156,423.3	351.3	11,452.4	(45,967.3)	122,259.7
Net income for the three months ended March 31, 2015	-	-	-	1,606.7	1,606.7
Issue of common shares upon vesting of share-based payment	410.3	-	(369.3)	-	41.0
Issue costs for subordinated convertible notes	-	(24.9)	-	-	(24.9)
Recognition of share-based payments	-	-	193.0	-	193.0
Balance at March 31, 2015	156,833.6	326.4	11,276.1	(44,360.6)	124,075.5
Net loss for the period April 1, 2015 to December 31, 2015	-	-	-	(18,927.3)	(18,927.3)
Issue of common shares	675.0	-	-	-	675.0
Issue of common shares upon vesting of share-based payment	327.0	-	(303.2)	-	23.8
Issue costs for subordinated convertible notes	-	-	-	-	-
Recognition of share-based payments	-	-	511.7	-	511.7
Balance at December 31, 2015	157,835.6	326.4	11,484.6	(63,287.9)	106,358.7
Net income for the three months ended March 31, 2016	-	-	-	28,486.9	28,486.9
Issue of common shares upon vesting of share-based payment	247.0	-	(234.6)	-	12.4
Recognition of share-based payments	-	-	183.1	-	183.1
Balance at March 31, 2016	158,082.6	326.4	11,433.1	(34,801.0)	135,041.1

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Conifex Timber Inc.

Condensed consolidated statement of cash flows
as at March 31, 2016 (unaudited)

(thousands of Canadian dollars)	Notes	3 months ended March 31,	
		2016	2015
		\$	\$
Cash flows from operating activities			
Net income		28,486.9	1,606.7
Items not affecting cash:			
Amortization		4,782.2	2,811.8
Change in mark-to-market value of lumber price derivatives		33.7	65.6
Change in reforestation obligations		1,720.7	1,332.6
Interest expense and accretion		2,546.1	1,268.1
Share based compensation		195.4	234.0
LDA accretion		(156.2)	-
Loss (gain) on disposal of assets		(28,968.1)	2.2
		8,640.7	7,321.0
Change in:			
Trade and other receivables		(239.0)	1,579.6
Prepaid expenses and deposits		(390.8)	2,373.0
Inventories		(10,207.2)	(13,428.3)
Accounts payable, accrued liabilities and other payables		2,663.7	(569.4)
Environmental liabilities		(12.0)	(31.5)
Employee liabilities		239.4	256.7
Net cash provided from (used in) operating activities		694.8	(2,498.9)
Cash flows from investing activities			
Additions to property, plant and equipment		(1,017.2)	(8,066.8)
Additions to long-term investments		(20.9)	-
Proceeds on disposal of assets		-	(2.2)
Net cash used in investing activities		(1,038.1)	(8,069.0)
Financing activities			
Financing fees		(133.2)	(50.4)
Repayment of long-term debt		(189.2)	(467.2)
Interest paid		(2,917.2)	(1,316.7)
Proceeds from construction loan		-	5,755.8
Proceeds from operating loans		5,431.4	6,854.6
Repayment of term loan		(2,718.4)	-
Proceeds of long-term debt		211.8	-
Net cash provided from (used in) financing activities		(314.8)	10,776.1
Net increase (decrease) in cash		(658.1)	208.2
Cash, beginning of period		18,448.6	11,890.0
Cash, end of period		17,790.5	12,098.2

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Conifex Timber Inc.

Notes to condensed consolidated interim financial statements

March 31, 2016 (unaudited)

(Tabular amounts expressed in thousands except per share amounts)

In these notes, "Conifex" or the "Company" means Conifex Timber Inc. and its subsidiaries.

1. GENERAL INFORMATION

The primary business of Conifex in its lumber segment includes timber harvesting, reforestation, forest management, sawmilling logs into lumber and wood chips, and value added lumber finishing. Conifex's lumber products are sold in the United States, Chinese, Canadian and Japanese markets. The primary activity in its bioenergy segment is the production of electricity for external sale under an Electricity Purchase Agreement and internal supply under a Load Displacement Agreement at the power generation plant at Mackenzie, BC.

Conifex is a publicly-traded company listed on the Toronto Stock Exchange under the symbol CFF. The Company is incorporated under the *Canada Business Corporations Act* and is headquartered in Vancouver, BC, Canada.

The address of its registered office is 1000 Cathedral Place, 925 West Georgia Street, Vancouver, BC V6C 3L2.

2. BASIS OF PREPARATION

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34 *Interim Financial Reporting* ("IAS 34") and do not include all of the information required for full annual financial statements. The condensed consolidated interim financial statements should be read in conjunction with the annual financial statements for the year ended December 31, 2015, which have been prepared in accordance with International Financial Reporting Standards ("IFRS").

3. SIGNIFICANT ACCOUNTING POLICIES

These condensed consolidated interim financial statements have been prepared using the significant accounting policies and methods of computation consistent with those applied in the Company's December 31, 2015 annual consolidated financial statements.

4. SEASONALITY OF OPERATIONS

The Company's fibre inventories exhibit seasonal swings as the Company increases log inventories during the fall and winter months to ensure adequate supply of fibre to its mills during the spring months when logging operations are largely curtailed due to road conditions.

The operating results of the bioenergy segment will experience variability as a result of the application of a "time of delivery factor" to electricity pricing which adds a seasonal effect to quarterly revenues. The lowest revenues are expected to be generated in the spring months and the highest in the fall and winter months of each year.

Conifex Timber Inc.

Notes to condensed consolidated interim financial statements

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(Tabular amounts expressed in thousands except per share amounts)

5. INVENTORIES

	March 31, 2016	December 31, 2015
	\$	\$
Lumber	25,695.8	22,510.8
Logs	22,378.6	15,408.7
Supplies	5,332.1	5,208.0
By-products	32.6	104.4
	53,439.1	43,231.9

The above inventory balances are stated after inventory write-downs from cost to net realizable value. Inventory has been written down at March 31, 2016 by \$267,471 (December 31, 2015 – \$652,638). Write-downs are included in cost of goods sold when incurred.

6. OPERATING LOANS

\$35 Million senior secured revolving asset backed credit facility

The Company entered into a three-year \$25 million senior secured revolving asset backed credit facility (the "Facility") with a Canadian chartered bank in April 2013. Under the terms of the Facility, amounts drawn and to be repaid are determined by a borrowing base calculation that fluctuates with eligible accounts receivable and inventory balances, net of specific reserves. Borrowings can be in Canadian or U.S. dollars. Interest rates on Canadian dollar borrowings are based on either banker's acceptances or the Canadian chartered bank prime rate, at the Company's option, plus an applicable margin.

In January 2016, the Company completed the renewal and amendment of the Facility for a further three-year term. The amendment increases the borrowing availability to \$35 million and extends the maturity date of the Facility to January 29, 2019.

The Facility is primarily secured by a first priority security interest on existing and future current assets of the lumber segment. The Company is subject to customary covenants, including a fixed charge coverage ratio if the amount available for borrowing falls below a certain threshold. Conifex uses the Facility primarily for working capital in its lumber segment and for other permitted general corporate purposes.

The Company has drawn \$14,050,000 of the Facility as at March 31, 2016 (December 31, 2015 – \$11,050,000).

Subsequent to the end of the quarter, in April 2016, the Company repaid the balance drawn against the Facility of \$14,050,000 (note 12).

Demand revolving loan and demand revolving line

Lignum Forest Products LLP ("Lignum"), a wholly-owned subsidiary of the Company, has a \$7.5 million demand revolving loan, a demand revolving line to a limit of \$975,000 for the purchase of forward exchange contracts, and a \$1 million manufacturer's advance facility to fulfill confirmed sales contracts for supply of lumber to foreign buyers (collectively, the "Revolving Loan"). The Revolving Loan bears interest at Canadian prime plus an applicable margin or U.S. base rate plus an applicable margin.

The Revolving Loan is secured by a general security agreement and a general assignment of Lignum's assets. Lignum is subject to customary covenants, including maintaining a debt to equity ratio, current ratio and tangible net worth above certain thresholds.

Conifex Timber Inc.

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(Tabular amounts expressed in thousands except per share amounts)

Lignum has drawn \$8,208,280 of the Revolving Loan as at March 31, 2016 (December 31, 2015 – \$5,776,868).

\$1.75 Million revolving operating facility

Conifex Power Limited Partnership (“CP Partnership”), a wholly-owned subsidiary of the Company, has a \$1.75 million revolving operating facility in connection with the project financing secured in November 2013 (note 7(d)).

As of March 31, 2016, CP Partnership has drawn \$1,500,000 of the revolving facility (December 31, 2015 - \$1,500,000).

7. BORROWINGS

	March 31, 2016	December 31, 2015
	\$	\$
Non-current		
Long term debt (a)	11.4	45.7
Senior secured notes (b)	24,594.8	24,357.7
Payment-in-kind note (c)	-	30,000.0
Term loan (d)	73,497.7	75,824.9
	98,103.9	130,228.3
Current		
Subordinated convertible notes (e)	11,850.5	11,797.7
Mortgage (f)	11,244.1	11,957.8
Current portion of long-term debt and term loan	4,019.1	4,353.3
	27,113.7	28,108.8
Total borrowings	125,217.6	158,337.1

(a) Secured loan facility sponsored by the Northern Development Initiative Trust

Long-term debt included a secured loan facility provided under the Community Adjustment Fund (“CAF”) loan program sponsored by the Northern Development Initiative Trust. The CAF loan carried a fixed interest rate of 3.75% and was repayable by 20 quarterly payments of \$485,700 commencing June 2011. The loan was secured by a General Security Agreement (excluding inventory and receivables) and a mortgage against certain properties. The Company repaid the remaining balance of \$83,296 during the three months ended March 31, 2016 (Year ended December 31, 2015 – \$1,895,051).

Long-term debt also includes three capital leases for mobile equipment. The capital leases expire in 2016 and 2017 and the principal outstanding at March 31, 2016 is \$326,792 (December 31, 2015 – \$220,825).

(b) Senior secured notes

In September 2013, the Company issued promissory notes (the “Notes”) in the aggregate principal amount of \$30 million. The Notes mature on September 18, 2017 and bear interest at a rate of 8% per annum. The Company may redeem the Notes, in whole or in part, upon 15 days’ notice and payment of interest accrued on the amount redeemed to the date of redemption, but otherwise at par. The Notes are primarily secured by a first priority security interest in certain long-term lumber assets.

On August 4, 2015, the Company redeemed \$4,000,000 of the issued notes. Subsequent to the end of the quarter, in April 2016, the Company redeemed an additional \$5,700,000 of the issued notes (note 12).

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(Tabular amounts expressed in thousands except per share amounts)

For the three months ended March 31, 2016, the Company recorded expenses that comprised accretion of \$225,718, amortization of issuance costs of \$11,383 and interest expense of \$518,575 (year ended December 31, 2015 – \$902,873, \$45,534 and \$2,268,493 respectively).

(c) Payment-in-kind note

In August 2015, the Company's wholly-owned subsidiary, Conifex Inc., entered into an investment agreement, pursuant to which it issued a payment-in-kind note (the "PIK Note") in the principal amount of \$30 million. The PIK Note had a term of five years and had a maturity date of August 4, 2020. The PIK Note was non-interest bearing from the issue date until August 3, 2017.

On February 12, 2016, the holder of the PIK Note exercised its option to convert the PIK Note into an ownership interest in a forest license with 200,000 m³ of annual cut (the "Forest Licence"). The redemption of the PIK Note resulted in a gain on the sale of the Forest Licence of \$28.97 million. As a result of a tax election which was filed in 2015 to increase the tax basis of the Forest Licence, no current income tax arises on the PIK Note redemption in the year.

(d) Term loan

CP Partnership secured project financing (the "Project Financing") with a syndicate of four institutional lenders led by a Canadian chartered bank in November 2013. The Project Financing is for an aggregate up to \$102.7 million and includes a development and construction loan facility of \$82 million (the "Construction Facility"). The Construction Facility comprises floating rate and fixed rate tranches, both of which mature on July 31, 2015 (amended from June 30, 2015). On July 30, 2015, CP Partnership converted the Construction Facility into an amortized term loan (the "Term Loan") that matures on December 1, 2019. The balance of the Project Financing is in the form of a \$18.95 million letter of credit facility and a \$1.75 million revolving operating facility. The letter of credit facility is utilized primarily to secure certain obligations of CP Partnership under its Load Displacement Agreement and a debt service reserve fund.

Interest rates on the floating rate tranche borrowings are based on either banker's acceptances or the Canadian chartered bank prime rate, at CP Partnership's option, plus an applicable margin. The fixed rate tranche bears an interest rate largely consistent with the floating rate tranche.

The Project Financing is primarily secured by a first priority security interest on existing and after acquired assets of CP Partnership.

As at March 31, 2016, CP Partnership issued letters of credit totaling \$18,750,000 (December 31, 2015 - \$18,750,000) under the letter of credit facility provided under the Project Financing.

For the three months ended March 31, 2016, CP Partnership recorded interest expense of \$1,303,113 and financing expense of \$8,191 (year ended December 31, 2015 – \$3,510,166 and \$13,862 respectively). CP Partnership has repaid \$1,824,000 of the floating rate tranche and \$894,444 of the fixed rate tranche during the quarter (year ended December 31, 2015 - \$1,799,000 and \$281,111 respectively).

As at March 31, 2016, CP Partnership held \$10,418,801 of cash in restricted accounts (December 31, 2015 – \$8,545,653). Funds from restricted accounts are distributed in accordance with the terms of the Project Financing.

(e) Subordinated convertible notes

On December 15, 2014, the Company issued \$12,000,000 in unsecured subordinated convertible notes (the "Convertible Notes"). The Convertible Notes mature on December 15, 2016 and bear interest at a rate of 7% per annum. The Convertible Notes are convertible at the option of the holder into common shares at a conversion price of \$6.22 per share.

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Notes to condensed consolidated interim financial statements

March 31, 2016 (unaudited)

(Tabular amounts expressed in thousands except per share amounts)

For the three months ended March 31, 2016, the Company recorded expenses that comprised accretion of \$40,806, amortization of issuance costs of \$11,968 and interest expense of \$207,123 (year ended December 31, 2015 – \$167,105, \$49,128 and \$840,000 respectively).

(f) Mortgage

On August 6, 2015, the Company acquired idled sawmill assets located in El Dorado, Arkansas, United States (the "El Dorado Sawmill Assets"). Consideration paid for the acquired assets included a US\$8.64 million vendor mortgage (the "Mortgage"). The Mortgage bears interest at a rate of 6% per annum, payable quarterly beginning on November 1, 2015, and matures on the earlier of December 1, 2016 or the day before any remodel, construction or addition of buildings and/or equipment of the El Dorado Sawmill Assets. The Mortgage is secured against the El Dorado Sawmill Assets.

For the three months ended March 31, 2016, interest of \$177,854 (year ended December 31, 2015 - \$277,764) has been capitalized to the El Dorado Sawmill Assets.

8. INCOME TAX

The Company has not recognized current income tax expense during the first quarter of 2016 as the Company had non-capital loss carry forwards totalling approximately \$32.1 million as at December 31, 2015. Due to the cyclical nature of the wood products industry and the economic conditions over the last several years, the Company has not recognized the benefits of its deferred tax assets available to reduce future taxable income.

9. SEGMENT INFORMATION

The Company is organized into business units based on its products and services and has two reportable segments:

- Lumber - The main activities of the lumber segment include timber harvesting, reforestation, forest management, sawmilling logs into lumber and wood chips, and value added lumber finishing. The Company markets and distributes its lumber products through its wholly-owned subsidiaries, Conifex Fibre Marketing Inc. ("CFMI"), Lignum, and Navcor Transportation Services Inc. ("Navcor"). CFMI, Lignum, and Navcor generate additional revenue from third party transactions.
- Bioenergy - The primary activities of the bioenergy segment are the generation of electrical power and the development of other opportunities in bioenergy and bioproducts which are complementary to the Company's harvesting and manufacturing operations. The Mackenzie power generation plant commenced commercial operations on May 1, 2015.

Conifex Timber Inc.

Notes to condensed consolidated interim financial statements

March 31, 2016 (unaudited)

(Tabular amounts expressed in thousands except per share amounts)

Summary by segment:

	Lumber	Bioenergy	Corporate & other	Consolidated
	\$	\$	\$	\$
3 months ended March 31, 2016				
Sales to external customers	91,796.5	7,718.0	-	99,514.5
Operating income (loss)	1,171.6	2,630.9	(770.7)	3,031.8
Gain on disposal of assets	28,968.1	-	-	28,968.1
Interest expense and accretion	-	(1,311.3)	(1,234.8)	(2,546.1)
Other income	132.4	-	-	132.4
Foreign exchange loss	-	-	(1,099.3)	(1,099.3)
Net income (loss)	30,272.1	1,319.6	(3,104.8)	28,486.9
Amortization	3,190.1	1,578.3	13.8	4,782.2
Capital expenditures	529.5	128.2	296.8	954.5
Identifiable assets	190,094.2	127,284.5	19,948.1	337,326.8

	Lumber	Bioenergy	Corporate & other	Consolidated
	\$	\$	\$	\$
3 months ended March 31, 2015				
Sales to external customers	85,262.9	-	-	85,262.9
Operating income (loss)	1,998.5	(6.0)	(915.2)	1,077.3
Loss on disposal of assets	(2.2)	-	-	(2.2)
Interest expense and accretion	-	-	(1,268.1)	(1,268.1)
Other expense	(85.3)	-	-	(85.3)
Foreign exchange gain	-	-	1,885.0	1,885.0
Net income (loss)	1,911.0	(6.0)	(298.3)	1,606.7
Amortization	2,796.3	-	15.5	2,811.8
Capital expenditures	2,478.4	5,636.5	2.4	8,117.3
Identifiable assets	163,502.2	132,749.2	15,289.3	311,540.7

Revenues by geographic area were as follows:

	Three months ended March 31,	
	2016	2015
	\$	\$
United States	55,924.5	43,996.7
Canada	24,787.3	19,890.2
China	8,143.3	13,298.8
Japan	7,912.0	6,655.9
Other	2,747.3	1,421.3
	99,514.5	85,262.9

All of the Company's harvesting and manufacturing operations are located in the interior region of British Columbia.

Conifex Timber Inc.

Notes to condensed consolidated interim financial statements

March 31, 2016 (unaudited)

(Tabular amounts expressed in thousands except per share amounts)

10. FINANCIAL INSTRUMENTS

The Company's accounts receivable, other deposits and advances, notes payable, accounts payable and accrued liabilities, and long-term debt are measured at amortized cost subsequent to initial recognition.

Cash and cash equivalents and derivative instruments are measured at fair value.

Financial assets and liabilities that are measured subsequent to initial recognition at fair value are classified within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).

Level 3 - Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

The following table summarizes the Company's financial instruments at March 31, 2016 and December 31, 2015, and shows the level within the fair value hierarchy in which they have been classified (for financial instruments measured at fair value):

	Fair value hierarchy Level	March 31, 2016	December 31, 2015
		\$	\$
Financial assets			
Held for trading			
Derivative financial instruments	Level 2	558.7	872.3
		558.7	872.3

11. RECLASSIFICATION OF COMPARATIVE AMOUNTS

Certain comparative amounts for the prior year have been reclassified to conform to the current year's presentation.

12. EVENTS AFTER THE REPORTING PERIOD

On April 12, 2016, the Company entered into a timber harvesting cooperation agreement with a regional lumber manufacturer (the "Harvesting Partner") to conduct coordinated joint timber harvesting operations. Pursuant to the agreement, the Harvesting Partner paid \$20 million to acquire 50% of the issued and outstanding shares of a Conifex subsidiary which holds a forest licence with an annual timber harvest of 300,000 m³.

The net proceeds from the transaction were used to redeem \$5.7 million of the issued Notes (note 7(b)) and to repay \$14.05 million drawn on the Facility (note 6).