CANFOR PULP PRODUCTS INC.

CANFOR PULP LIMITED PARTNERSHIP

Condensed Consolidated Financial Statements

(unaudited)

For the three and six months ended June 30, 2011

Canfor Pulp Products Inc.
Condensed Balance Sheets
(unaudited)

(thousands of dollars)		**As at June 30, 2011**		As at December 31, 2010
ASSETS				
Current assets				
Cash and cash equivalents	**$**	**29,892**	$	-
Distributions receivable from Canfor Pulp Limited Partnership (note 7)		**8,163**		19,521
Total current assets		**38,055**		19,521
Equity investment in Canfor Pulp Limited Partnership (note 6)		**236,863**		240,425
	$	**274,918**	$	259,946
LIABILITIES				
Current liabilities				
Due to Canfor Pulp Limited Partnership (note 7)	**$**	**1,051**	$	-
Distributions payable		**-**		19,521
Income taxes payable		**10,512**		-
Total current liabilities		**11,563**		19,521
Fund units (note 5)		**-**		509,687
Deferred income tax liability (note 8)		**32,098**		52,854
	$	**43,661**	$	582,062
SHAREHOLDERS' EQUITY (DEFICIT)				
Unitholders' deficit (note 5)	**$**	**-**	$	(322,116)
Shareholders' capital (note 5)		**509,687**		-
Retained earnings (deficit)		**(278,430)**		-
Total Shareholders' equity (deficit)		**231,257**		(322,116)
	$	**274,918**	$	259,946

Subsequent event (note 10)

Canfor Pulp Products Inc.
Condensed Statements of Comprehensive Income (loss)
(unaudited)

(thousands of dollars, except unit and per unit amounts)	Three months ended **June 30, 2011**	 June 30, 2010	Six months ended **June 30, 2011**	 June 30, 2010
Income				
Equity income in Canfor Pulp Limited Partnership	**$ 24,023**	$ 21,681	**$ 49,250**	$ 38,154
Interest Income	**69**	-	**77**	-
Total income	**24,092**	21,681	**49,327**	38,154
Cost and expenses				
Administrative expenses (note 7)	**74**	-	**1,051**	-
Increase in amortized cost of Fund units (note 5)	**-**	75,956	**-**	200,182
Financing expense - distributions declared	**-**	18,457	**-**	29,815
	74	94,413	**1,051**	229,997
Net income (loss) before income taxes	**24,018**	(72,732)	**48,276**	(191,843)
Income tax expense (recovery) (note 8)	**6,264**	(928)	**(10,103)**	(1,198)
Net income (loss)	**$ 17,754**	$ (71,804)	**$ 58,379**	$ (190,645)
Equity interest in other comprehensive loss related to actuarial losses of Canfor Pulp Limited Partnership	**(535)**	(3,873)	**(636)**	(8,596)
Income tax recovery of other comprehensive loss related to actuarial losses of Canfor Pulp Limited Partnership	**140**	-	**140**	-
Comprehensive income (loss)	**$ 17,359**	$ (75,677)	**$ 57,883**	$ (199,241)
Net income (loss) per share/unit, basic and diluted	**$ 0.50**	$ (2.02)	**$ 1.64**	$ (5.37)
Weighted average number of shares/units (note 4)	**35,493,307**	35,493,307	**35,493,307**	35,493,307

Canfor Pulp Products Inc.
Condensed Statements of Changes in Equity
(unaudited)

(thousands of dollars)	Three months ended June 30, 2011	Three months ended June 30, 2010	Six months ended June 30, 2011	Six months ended June 30, 2010
Share capital (unitholders' capital)				
Balance beginning of period	**$ 509,687**	$ -	**$ -**	$ -
Corporate conversion	**-**	-	**509,687**	-
Balance at end of period	**$ 509,687**	$ -	**$ 509,687**	$ -
Retained earnings (deficit)				
Balance beginning of period	**$ (281,592)**	$ (240,176)	**$ (322,116)**	$ (116,612)
Net income (loss) for the period	**17,754**	(71,804)	**58,379**	(190,645)
Defined benefit plan actuarial losses of the Partnership included in other comprehensive income	**(535)**	(3,873)	**(636)**	(8,596)
Income tax recovery in other comprehensive loss related to actuarial losses of Canfor Pulp Limited Partnership	**140**	-	**140**	-
Dividends paid during the period	**(14,197)**	-	**(14,197)**	-
Balance at end of period	**$ (278,430)**	$ (315,853)	**$ (278,430)**	$ (315,853)
Total equity (deficit)	**$ 231,257**	**$** (315,853)	**$ 231,257**	$ (315,853)

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

Canfor Pulp Products Inc.
Condensed Statements of Cash Flows
(unaudited)

(thousands of dollars)	Three months ended **June 30, 2011**	Three months ended June 30, 2010	Six months ended **June 30, 2011**	Six months ended June 30, 2010
Cash generated from (used in)				
Operating activities				
Net income (loss) before tax	**$ 24,018**	$ (72,732)	**$ 48,276**	$ (191,843)
Items not affecting cash:				
Equity income in Canfor Pulp Limited Partnership	**(24,023)**	(21,681)	**(49,250)**	(38,154)
Increase in amortized cost of Fund units	-	75,956	-	200,182
Financing expense (distributions declared)	-	18,457	-	29,815
Distributions received from Canfor Pulp Limited Partnership	**25,557**	15,617	**63,533**	25,555
Cash flow from operations before working capital changes	**25,552**	15,617	**62,559**	25,555
Due to Canfor Pulp Limited Partnership	**74**	-	**1,051**	-
Net cash from operations	**25,626**	15,617	**63,610**	25,555
Financing activities				
Distributions paid to unitholders	**$ -**	$ (15,617)	**$ (19,521)**	$ (25,555)
Dividends paid to shareholders	**(14,197)**	-	**(14,197)**	-
	(14,197)	(15,617)	**(33,718)**	(25,555)
Change in cash and cash equivalents	**$ 11,429**	$ -	**$ 29,892**	$ -
Beginning balance in cash and cash equivalents	**18,463**	-	-	-
Ending balance in cash and cash equivalents	**$ 29,892**	$ -	**$ 29,892**	$ -

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

1. General information and reporting entity

Canfor Pulp Products Inc. (CPPI) is domiciled in Canada and listed on the Toronto Stock Exchange. The address of CPPI's registered office is 1700 – 666 Burrard Street, Vancouver, British Columbia, Canada V6C 2X8. The unaudited financial statements (the financial statements) include the accounts of CPPI.

CPPI has been established to acquire and hold an interest in Canfor Pulp Limited Partnership (the Partnership). The Partnership produces and sells Northern Bleached Softwood Kraft (NBSK) Pulp and fully bleached, high performance Kraft Paper. The Partnership operations consist of two NBSK pulp mills and one NBSK pulp and paper mill located in Prince George, British Columbia and a marketing group based in Vancouver, British Columbia.

At June 30, 2011, Canadian Forest Products Ltd. (Canfor) owns 50.2% and CPPI owns 49.8% of the issued and outstanding units of the Partnership.

Corporate Conversion Arrangement

CPPI is a company formed on March 16, 2010. On January 1, 2011 Canfor Pulp Income Fund (the Fund) completed a plan of arrangement whereby the Fund unitholders exchanged their Fund units for common shares in CPPI on a one-for-one basis. The unitholders of the Fund became the sole shareholders of CPPI which became the sole owner of all of the outstanding Fund units. Immediately following the conversion, the Fund was wound up, CPPI received all of the assets and assumed all of the liabilities of the Fund and CPPI became the direct holder of the 49.8% interest in the Partnership previously held by the Fund.

The financial statements have been prepared on a continuity of interest basis, which recognizes CPPI as the successor entity to the Fund. As a result, in current and future financial statements and Management's Discussion and Analysis, CPPI will refer to common shares, shareholders and dividends which were formerly referred to as units, unitholders and distributions under the trust structure; comparative amounts will reflect the history of the Fund.

2. Basis of preparation and adoption of IFRS

Statement of Compliance and Conversion to International Financial Reporting Standards

CPPI prepares its financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants (CICA Handbook). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards (IFRS), and require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, CPPI has commenced reporting on this basis in its 2011 interim consolidated financial statements. In these financial statements, the term "Canadian GAAP" refers to Canadian GAAP before the adoption of IFRS.

These financial statements have been prepared in accordance with International Accounting Standard (IAS) 34, Interim Financial Reporting and IFRS 1, using accounting policies consistent with IFRS as issued by the International Accounting Standards Board (IASB) and interpretations of the International Financial Reporting Interpretations Committee (IFRIC). The accounting policies followed in these financial statements are the same as those applied in the interim financial statements for the period ended March 31, 2011.

CPPI has consistently applied the same accounting policies throughout all periods presented, as if these policies had always been in effect. Note 5 discloses the impact of the transition to IFRS on CPPI's equity as at June 30, 2010 and statements of comprehensive income (loss) for the three and six months ended June 30, 2010, including the nature and effect of significant changes in accounting policies from those used in CPPI's financial statements for the year ended December 31, 2010 under Canadian GAAP.

The policies applied in these financial statements are based on IFRS issued and effective as of July 21, 2011, the date the Board of Directors approved the statements. Any subsequent changes to IFRS that are given effect in CPPI's annual financial statements for the year ending December 31, 2011 could result in restatement of these financial statements, including the transition adjustments recognized on change-over to IFRS. The financial statements should be read in conjunction with CPPI's Canadian GAAP annual financial statements for the year ended December 31, 2010 and CPPI's interim consolidated financial statements for the quarter ended March 31, 2011, prepared in accordance with IFRS applicable to interim financial statements.

3. New Accounting Pronouncements

The following IFRS have been issued by the International Accounting Standards Board, and adopted for use in Canada by the Accounting Standards Board, effective for annual periods beginning on or after January 1, 2013. CPPI has not applied these new standards as their use is not yet mandatory:

IFRS 9 – Financial Instruments

IFRS 10 – Consolidated Financial Statements

IFRS 11 – Joint Arrangements

IFRS 12 – Disclosure of Interests in Other Entities

IFRS 13 – Fair Value Measurement

IAS 27 – Separate Financial Statements

Amended IAS 19 – Employee Benefits

Amended IAS 28 – Investments in Associates

These new standards have not yet been adopted and CPPI has not completed assessing the impact that the new and amended standards may have on its financial statements or whether to proceed with early adoption of any of the new requirements.

4. Net Income per Share

Basic net income per Share is based on the weighted average number of Shares outstanding during the year. At June 30, 2011 and December 31, 2010 the Partnership had 35,776,483 Class B Exchangeable Limited Partnership Units outstanding which can be exchanged for Shares of CPPI at the option of the holder Canfor. Any issuance of new Shares as a result of such an exchange would be accompanied by a corresponding increase in CPPI's investment in the Partnership through the acquisition of Class B Exchangeable Limited Partnership Units. As a result, this potential conversion would not result in any dilution of CPPI's net income per share.

5. Reconciliations between IFRS and Canadian GAAP

The following reconciliations provide a quantification of the material impacts of the transition to IFRS on the Fund before the conversion of the Fund into a corporation (note 1).

Reconciliation of equity at June 30, 2010

(thousands of dollars, unaudited)		June 30, 2010
Previous Canadian GAAP – Total equity	$	235,222
Fund units [1]		(510,749)
CPPI share of Partnership IFRS transition adjustments [2]		(14,051)
Deferred income taxes [3]		(18,154)
Effect of the increase in equity income from the Partnership under IFRS		501
Effect of the increase in CPPI's share in the Partnership's other comprehensive loss under IFRS		(8,622)
IFRS – Total equity (deficit)	$	(315,853)

Reconciliation of comprehensive income (loss) for the three months ended June 30, 2010

(thousands of dollars, unaudited)		Three months ended June 30, 2010
Comprehensive income previous Canadian GAAP	$	22,162
Effect of the increase in equity income from the Partnership under IFRS		251
Fund units [1]		(75,956)
Distributions classified as a financing expense [1]		(18,457)
Deferred income taxes [3]		247
Effect of the increase in CPPI's share in the Partnership's other comprehensive loss under IFRS		(3,924)
Comprehensive loss - IFRS	$	(75,677)

Reconciliation of comprehensive income (loss) for the six months ended June 30, 2010

(thousands of dollars, unaudited)		Six months ended June 30, 2010
Comprehensive income previous Canadian GAAP	$	38,679
Effect of the increase in equity income from the Partnership under IFRS		501
Fund units [1]		(200,182)
Distributions classified as a financing expense [1]		(29,815)
Deferred income taxes [3]		198
Effect of the increase in CPPI's share in the Partnership's other comprehensive loss under IFRS		(8,622)
Comprehensive loss - IFRS	$	(199,241)

Notes to the Reconciliations

1) **IAS 32 Classification** - Under Canadian GAAP the Fund units were classified as equity. IAS 32 requires that the Fund units be classified as a financial liability under IFRS prior to conversion to a corporation. Under the terms of the Fund's trust indenture, unitholders had a puttable option, whereby the Fund would have been required to redeem Fund units at the request of the unitholder and required the Fund to distribute all of the taxable income received from the Partnership. In addition, the Fund's distributions were classified as a financing expense recorded in the statement of comprehensive income. The liability was recorded at amortized cost with changes recorded in the statement of comprehensive income. Upon conversion to a corporation effective January 1, 2011, the Fund units were converted on a one-for-one basis into shares of CPPI and the shares are classified as equity with dividends treated as an equity distribution.

2) **Canfor Pulp Limited Partnership conversion** – As a result of a change in accounting policies for the Partnership due to the conversion to IFRS, CPPI's equity income, investment and other comprehensive income has been restated. For further details on the impact of the transition on the Partnership see the Partnership's disclosure on pages 15 through 17.

3) **IAS 12 tax rate** - Under Canadian GAAP the Fund recorded temporary tax differences that were projected to reverse after 2010 based on specified investment flow through entity (SIFT) tax rates. However, IAS 12 requires that companies should use the undistributed rate for recording taxes. Therefore, under IFRS the rate to apply to temporary differences that are projected to reverse after 2010 would be the highest marginal personal tax rate (43.7%) rather than the SIFT rate. The highest marginal personal tax rate is the rate at which tax would be payable by the Fund should distributions not be declared. Subsequent to January 1, 2011 as a result of the conversion of the Fund into a corporation, the temporary tax differences are to be measured at the expected corporate tax rate (25.0%) at the time of reversal.

6. Equity Investment in Canfor Pulp Limited Partnership

CPPI's equity investment in the Partnership is as follows:

(thousands of dollars, unaudited)		**Six months ended June 30, 2011**		Year ended December 31, 2010
Balance, beginning of period	**$**	**240,425**	$	249,593
Equity interest in income of the Partnership		**49,250**		89,166
Equity interest in other comprehensive loss of the Partnership		**(636)**		(6,761)
Distributions from the Partnership		**(52,176)**		(91,573)
Balance, end of period	**$**	**236,863**	$	240,425

7. Related Party Transactions

All accounting, treasury, legal and administrative functions for CPPI are performed on its behalf by the Partnership pursuant to a support agreement. The value of these services during the second quarter of 2011 was $74,000 and was included as an administrative expense of CPPI with the balance of $1.1 million outstanding as an accounts payable to the Partnership at June 30, 2011.

Distributions earned from the Partnership for the three months ended June 30, 2011 were $24.5 million of which $16.3 million was received, with the balance of $8.2 million receivable on June 30, 2011.

8. Income Taxes

Immediately prior to converting to a corporation on January 1, 2011, the Fund, as a publicly traded income trust, was to be taxed on income starting in 2011, similarly to rules applying to corporations.

(thousands of dollars, unaudited)		**Three months ended** **June 30, 2011**		June 30, 2010		**Six months ended** **June 30, 2011**		June 30, 2010
Current	**$**	**5,548**	$	-	**$**	**10,512**	$	-
Deferred		**716**		(928)		**(20,615)**		(1,198)
Income tax expense (recovery)	**$**	**6,264**	$	(928)	**$**	**(10,103)**	$	(1,198)

The following table reconciles the income tax expense calculated using statutory tax rates to the actual income tax expense.

(thousands of dollars, unaudited)		Three months ended **June 30, 2011**		Six months ended **June 30, 2011**
Income tax expense at statutory rate 2011 – 26.5% (2010 – nil)	$	6,365	$	12,793
Add (deduct):				
Permanent difference from capital gains on translation of US denominated debt & other non deductible items		(101)		(270)
Change in SIFT tax rate (note 5)		-		(22,626)
	$	6,264	$	(10,103)

9. Segmented Information

CPPI operates in one industry segment, namely investing in pulp and paper producing assets in one geographic region, Canada.

10. Subsequent Event

Subsequent to the period end, dividends were declared in the amount of $0.40 per share to be paid on August 9, 2011 to shareholders of record at the close of business on August 2, 2011.

Canfor Pulp Limited Partnership
Condensed Consolidated Balance Sheets
(unaudited)

(millions of dollars)		**As at June 30, 2011**		As at December 31, 2010
ASSETS				
Current assets				
Cash and cash equivalents	**$**	**26.5**	$	64.2
Accounts receivable (note 10)				
Trade		**122.8**		108.0
Other		**14.0**		14.8
Green Transformation Program (note 13)		**27.6**		17.9
Inventories (note 7)		**130.2**		123.4
Prepaid expenses and other assets		**5.9**		11.0
Total current assets		**327.0**		339.3
Non-current assets				
Property, plant and equipment (note 5)		**496.0**		513.5
Other long-term assets		**0.5**		0.5
	$	**823.5**	$	853.3
LIABILITIES				
Current liabilities				
Accounts payable and accrued liabilities	**$**	**142.8**	$	139.3
Distributions payable		**16.4**		39.2
Total current liabilities		**159.2**		178.5
Non-current liabilities				
Long-term debt (note 9)		**106.1**		109.4
Post employment benefits (note 8)		**79.7**		79.8
Long-term provisions		**3.2**		3.1
Total liabilities	**$**	**348.2**	$	370.8
PARTNERS' EQUITY				
Partnership units (note 6)		**587.5**		587.5
Cumulative distributions in excess of income		**(112.2)**		(105.0)
Total Partners' equity		**475.3**		482.5
	$	**823.5**	$	853.3

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

Canfor Pulp Limited Partnership
Condensed Consolidated Statements of Comprehensive Income
(Unaudited)

(millions of dollars, except units and per unit amounts, unaudited)	Three months ended June 30, 2011	Three months ended June 30, 2010	Six months ended June 30, 2011	Six months ended June 30, 2010
Revenue				
Sales	**$ 242.1**	$ 247.6	**$ 494.4**	$ 487.1
	242.1	247.6	**494.4**	487.1
Costs and expenses				
Manufacturing and product costs	**142.8**	141.1	**291.8**	293.8
Freight and other distribution costs	**28.7**	29.8	**59.4**	60.9
Amortization	**15.0**	17.2	**31.5**	33.5
Selling and administration costs	**6.5**	7.4	**12.7**	13.8
	193.0	195.5	**395.4**	402.0
Operating income	**49.1**	52.1	**99.0**	85.1
Interest expense	**(1.9)**	(1.9)	**(4.0)**	(3.9)
Foreign exchange gain (loss) on long-term debt	**0.8**	(5.0)	**3.3**	(1.6)
Gain (loss) on derivative financial instruments	**1.0**	(3.8)	**2.6**	(3.4)
Foreign exchange gain (loss) on working capital	**(0.7)**	2.1	**(1.8)**	0.3
Other income (expense)	**(0.1)**	0.1	**(0.2)**	0.1
	(0.9)	(8.5)	**(0.1)**	(8.5)
Net income	**48.2**	43.6	**98.9**	76.6
Other comprehensive income	**-**	0.1	**-**	0.1
Actuarial losses recognized in accumulated distributions in excess of income	**(1.1)**	(7.9)	**(1.3)**	(17.3)
Total comprehensive income	**$ 47.1**	$ 35.8	**$ 97.6**	$ 59.4
Net income per Partnership unit, basic and diluted	**$ 0.68**	$ 0.61	**$ 1.39**	$ 1.07
Weighted average Partnership units outstanding	**71,270,025**	71,270,025	**71,270,025**	71,270,025

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

Canfor Pulp Limited Partnership
Condensed Consolidated Statements of Changes in Equity
(Unaudited)

(millions of dollars)	Three months ended June 30, 2011	Three months ended June 30, 2010	Six months ended June 30, 2011	Six months ended June 30, 2010
Partnership units				
Balance at beginning and end of period	**$ 587.5**	$ 587.5	**$ 587.5**	$ 587.5
Cumulative distributions in excess of income				
Balance beginning of period	**$ (110.1)**	$ (85.8)	**$ (105.0)**	$ (86.6)
Net income for the period	**48.2**	43.6	**98.9**	76.6
Defined benefit plan actuarial losses	**(1.1)**	(7.9)	**(1.3)**	(17.3)
Other comprehensive income	**-**	0.1	**-**	0.1
Distributions declared during the period (note 12)	**(49.2)**	(37.1)	**(104.8)**	(59.9)
Balance at end of period	**$ (112.2)**	$ (87.1)	**$ (112.2)**	$ (87.1)
Total equity	**$ 475.3**	$ 500.4	**$ 475.3**	$ 500.4

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

Canfor Pulp Limited Partnership
Condensed Consolidated Statements of Cash Flows
(Unaudited)

(millions of dollars)	Three months ended June 30, 2011	Three months ended June 30, 2010	Six months ended June 30, 2011	Six months ended June 30, 2010
Cash and cash equivalents generated from (used in)				
Operating activities				
Net income	**$ 48.2**	$ 43.6	**$ 98.9**	$ 76.6
Adjustments for:				
Amortization	**15.0**	17.2	**31.5**	33.5
Unrealized foreign exchange loss (gain) on long-term debt	**(0.8)**	5.0	**(3.3)**	1.6
Interest expense	**1.9**	1.9	**4.0**	3.9
Reduction (increase) in value of outstanding derivative instruments	**(1.4)**	3.3	**(1.8)**	4.5
Employee future benefits	**1.4**	1.4	**2.7**	2.9
Other	**(0.1)**	0.1	**0.2**	0.1
Salary pension plan contribution	**(2.1)**	(0.6)	**(4.1)**	(1.2)
Cash flow from operations before working capital changes	**62.1**	71.9	**128.1**	121.9
Decrease (increase) in non-cash working capital				
Accounts receivable – trade and other	**(15.4)**	(15.6)	**(12.9)**	(28.8)
Inventories	**(13.9)**	(9.7)	**(6.7)**	(3.0)
Prepaid expenses and other assets	**3.3**	0.1	**5.1**	(1.0)
Accounts payable and accrued liabilities	**2.3**	7.5	**-**	12.9
Net cash from operations	**38.4**	54.2	**113.6**	102.0
Financing activities				
Distributions paid to partners	**(51.3)**	(31.4)	**(127.6)**	(51.3)
Interest paid	**(3.3)**	(3.7)	**(3.6)**	(3.9)
Net cash used in financing	**(54.6)**	(35.1)	**(131.2)**	(55.2)
Investing activities				
Property, plant and equipment	**(10.3)**	(11.9)	**(17.1)**	(18.4)
Green Transformation Program expenditures	**(20.2)**	(1.6)	**(36.9)**	(1.6)
Green Transformation Program reimbursements	**21.6**	-	**31.2**	-
Government grants received	**0.9**	-	**2.7**	-
Net cash used in investing	**(8.0)**	(13.5)	**(20.1)**	(20.0)
Increase (decrease) in cash and cash equivalents	**(24.2)**	5.6	**(37.7)**	26.8
Cash and cash equivalents, beginning of period	**50.7**	34.7	**64.2**	13.5
Cash and cash equivalents, end of period	**$ 26.5**	$ 40.3	**$ 26.5**	$ 40.3

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

Notes to the Condensed Consolidated Financial Statements as at June 30, 2011
(Unaudited, in millions of dollars unless otherwise noted)

1. General information and reporting entity

Canfor Pulp Limited Partnership (the Partnership) is a limited Partnership formed on April 21, 2006, under the laws of Manitoba, to acquire and carry on the NBSK pulp and paper business of Canadian Forest Products Ltd. a subsidiary of Canfor Corporation (collectively Canfor). The Partnership is domiciled in Canada. The address of the Partnership's registered office is 230-1700 West 75th Avenue, Vancouver, British Columbia, Canada V6P 6G2. The consolidated interim financial statements (the financial statements) include the accounts of the Partnership and its subsidiaries.

The Partnership is a producer of market NBSK Pulp and fully bleached, high performance Kraft Paper. The Partnership consists of two NBSK pulp mills and one NBSK pulp and paper mill located in Prince George, British Columbia and a marketing group based in Vancouver, British Columbia (the Pulp Business).

At June 30, 2011, Canfor owns 50.2% and Canfor Pulp Products Inc. (CPPI) owns 49.8% of the issued and outstanding units of the Partnership.

Economic Dependence

The Partnership depends on Canfor to provide approximately 53% (2010 – 56%) of its fibre supply as well as to provide certain key business and administrative services as described in note 10. As a result of these relationships the Partnership considers its operations to be dependent on its ongoing relationship with Canfor.

2. Basis of preparation and adoption of IFRS

Statement of Compliance and Conversion to International Financial Reporting Standards

The Partnership prepares its financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants (CICA Handbook). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards (IFRS), and requires publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Partnership has commenced reporting on this basis in its 2011 interim consolidated financial statements. In these financial statements, the term Canadian GAAP refers to Canadian GAAP before the adoption of IFRS.

These financial statements have been prepared in accordance with International Accounting Standard (IAS) 34, Interim Financial Reporting and IFRS 1, using accounting policies consistent with IFRS as issued by the International Accounting Standards Board (IASB) and interpretations of the International Financial Reporting Interpretations Committee (IFRIC). The accounting policies followed in these financial statements are the same as those applied in the interim consolidated financial statements for the period ended March 31, 2011.

The Partnership has consistently applied the same accounting policies throughout all periods presented, as if these policies had always been in effect. Note 4 discloses the impact of the transition to IFRS on the Partnership's equity as at June 30, 2010 and statements of comprehensive income for the three and six months ended June 30, 2010, including the nature and effect of significant changes in accounting policies from those used in the Partnership's consolidated financial statements for the year ended December 31, 2010 under Canadian GAAP.

The policies applied in these financial statements are based on IFRS issued and effective as of July 21, 2011, the date the Board of Directors approved the statements. Any subsequent changes to IFRS that are given effect in the Partnership's annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these financial statements, including the transition adjustments recognized on change-over to IFRS. The financial statements should be read in conjunction with the Partnership's Canadian GAAP annual financial statements for the year ended December 31, 2010 and the Partnership's interim consolidated financial statements for the quarter ended March 31, 2011 prepared in accordance with IFRS applicable to interim financial statements.

3. New Accounting Pronouncements

The following IFRS have been issued by the International Accounting Standards Board, and adopted for use in Canada by the Accounting Standards Board, effective for annual periods beginning on or after January 1, 2013. The Partnership has not applied these new standards as their use is not yet mandatory:

IFRS 9 – Financial Instruments

IFRS 10 – Consolidated Financial Statements

IFRS 11 – Joint Arrangements

IFRS 12 – Disclosure of Interests in Other Entities

IFRS 13 – Fair Value Measurement

IAS 27 – Separate Financial Statements

Amended IAS 19 – Employee Benefits

Amended IAS 28 – Investments in Associates

These new standards have not yet been adopted and the Partnership has not completed assessing the impact that the new and amended standards may have on its financial statements or whether to proceed with early adoption of any of the new requirements.

4. Reconciliations between IFRS and Canadian GAAP

The following reconciliations provide a quantification of the effect of the transition to IFRS.

Reconciliation of equity at June 30, 2010

(millions of dollars, unaudited)	As at June 30, 2010	
Previous Canadian GAAP – Total equity	$	544.9
Recognition of unamortized actuarial losses at date of transition[1]		(28.2)
Lower pension expense for the six months ended June 30, 2010[1]		1.0
Actuarial losses on defined benefit plans for the six months ended June 30, 2010[1]		(17.3)
IFRS – Total equity	**$**	**500.4**

Reconciliation of comprehensive income for three months ended June 30, 2010

(millions of dollars, unaudited)	Three months ended June 30, 2010	
Comprehensive income - Previous Canadian GAAP	$	**43.2**
Lower pension expense for period[1]		0.5
	$	**43.7**
Actuarial losses on defined benefit plans during the period[1]	$	(7.9)
Comprehensive income IFRS	**$**	**35.8**

Reconciliation of comprehensive income for six months ended June 30, 2010

(millions of dollars, unaudited)		Six months ended June 30, 2010
Comprehensive income - Previous Canadian GAAP	$	75.7
Lower pension expense for period[1]		1.0
	$	76.7
Actuarial losses on defined benefit plans during the period[1]		(17.3)
Comprehensive income IFRS	**$**	59.4

Notes to the Reconciliations

1) **Employee Benefits** - Under IFRS the Partnership's accounting policy is to recognize all actuarial gains and losses immediately in other comprehensive income. At the date of transition, all previously unrecognized cumulative actuarial gains and losses and unrecognized past service costs were recognized in equity. The impact of this policy decision was a $28.2 million decrease in equity, an $11.2 million decrease in other long-term assets and a $17.0 million increase to long-term liabilities.

   All actuarial gains and losses arising in 2010 were recognized in other comprehensive income. A charge to accumulated earnings and distributions of $17.3 million for actuarial losses related to the six months ended June 30, 2010 was recorded (second quarter of 2010 a charge of $7.9 million was recorded to accumulated earnings and distributions). As a result of immediate recognition of previously unrecognized cumulative actuarial gains and losses the total pension expense for the six months ended was reduced by $1.0 million under IFRS (second quarter of 2010 employee benefits expense was $0.5 million lower than previously reported). This reduced manufacturing costs by $1.0 million for the six months ended June 30, 2010 (reduced manufacturing costs for the second quarter of 2010 by $0.5 million).

2) **Property, plant and equipment (PP&E)** – For major maintenance, International Accounting Standard (IAS) 16 requires for major inspections and overhauls to be accounted as a separate component of PP&E. The Partnership has determined that a significant part of its major maintenance program qualifies as a separate component of PP&E under IFRS. As at January 1, 2010 the resulting impact is a $20.7 million increase to PP&E, a $15.3 million decrease to prepaid expenses and a $5.4 million decrease to other long-term assets.

   The impact on net income for the six months ended June 30, 2010 was an increase in amortization of $9.9 million with an offsetting decrease to manufacturing costs. The impact on the second quarter of 2010 was an increase in amortization of $5.2 million with an offsetting decrease to manufacturing costs.

   The change in policy also increased the reported capital expenditures in the statements of cash flows by $11.5 million for the six months ended June 30, 2010 and $5.9 million for the quarter ended June 30, 2010 restated to conform to IFRS. The long-term maintenance provision and long-term maintenance expenditure line items on the consolidated statements of cash flows are no longer applicable and those amounts are now included in PP&E.

3) **Statement of cash flows (interest received / paid) –** Under IFRS an accounting policy choice is available as to where interest and distributions paid and interest and distributions received are presented in the statements of cash flows. The Partnership has elected to present distributions paid to partners and interest paid in financing activities and interest received in investing activities. Under Canadian GAAP interest received and paid were presented within operating activities.

4) **Reclassification of Employee Future Benefits and Asset Retirement Obligations** – Under Canadian GAAP employee pension obligations, other retirees benefits and asset retirement obligations were included in long-term liabilities. Under IFRS, pension and other retirees benefits have been classified on the consolidated balance sheets as post employment benefits and asset retirement obligations have been included in long-term provisions.

5. Property, Plant and Equipment

	June 30, 2011		
(millions of dollars, unaudited)	Cost	Accumulated amortization	Net
Land and improvements	**5.4**	**-**	**5.4**
Asset retirement - Landfill	**2.3**	**0.9**	**1.4**
Buildings, machinery and equipment	**1,363.7**	**889.9**	**473.8**
Major Maintenance	**34.7**	**22.7**	**12.0**
Construction in progress	**3.4**	**-**	**3.4**
	1,409.5	**913.5**	**496.0**

	December 31, 2010		
(millions of dollars, unaudited)	Cost	Accumulated amortization	Net
Land and improvements	5.4	-	5.4
Asset retirement - Landfill	2.3	0.9	1.4
Buildings, machinery and equipment	1,356.1	867.0	489.1
Major Maintenance	37.0	23.1	13.9
Construction in progress	3.7	-	3.7
	1,404.5	891.0	513.5

6. Net Income per Partnership Unit

Basic net income per Partnership unit is based on the weighted average number of Limited Partnership units outstanding during the period. All outstanding Partnership units were issued on July 1, 2006, and there was no change in the number of outstanding Partnership units during the quarter.

7. Inventories

(millions of dollars, unaudited)	**June 30, 2011**	December 31, 2010
Pulp	**66.8**	52.7
Paper	**11.3**	10.1
Wood chips	**8.2**	16.4
Processing materials and supplies	**43.9**	44.2
	130.2	123.4

8. Employee Future Benefits

The Partnership, in participation with Canfor, has funded and unfunded defined benefit plans, as well as a defined contribution plan, that provide pension, other retirement and post-employment benefits to substantially all salaried employees and for its hourly employees covered under collective agreements. The defined benefit plans are based on years of service and final average salary. The post-employment benefit plans are non-contributory and include a range of health care and other benefits.

Total employee future benefit expenses were as follows:

(millions of dollars, unaudited)	Three months ended June 30, 2011	June 30, 2010	Six months ended June 30, 2011	June 30, 2010
Pension plans	**1.0**	1.1	**2.0**	2.1
Other employee future benefit plans	**1.2**	1.0	**2.4**	2.1
Contributions to forest industry union plans	**1.8**	1.7	**3.4**	3.3
	4.0	3.8	**7.8**	7.5

9. Credit Facilities and Long-term Debt

At June 30, 2011 the Partnership had outstanding long-term debt of $106.1 million (December 31, 2010 – $109.4 million, US$110.0 million) in the form of unsecured US dollar private placement notes (the Notes). The Notes bear interest at 6.41% and are repayable in full on their maturity date of November 30, 2013.

The Partnership has a $40.0 million bank credit facility with a maturity date of November 30, 2013, of which $0.5 million was utilized at June 30, 2011 for a standby letter of credit issued for general business purposes. In addition, the Partnership has a separate facility with a maturity date of November 30, 2013, to cover the $13.0 million standby letter of credit issued to BC Hydro under the Electricity Purchase Agreement. The Partnership also has an undrawn $30.0 million bridge loan credit facility with a maturity date of December 31, 2012 to fund timing differences between expenditures and reimbursements for projects funded under the Canadian Federal Government Green Transformation Program. Interest and other costs of the credit facilities are at prevailing market rates. The leverage ratio and interest coverage ratio are consistent with the financial covenants under the Note Agreement.

The Notes and bank credit agreements each contain similar financial covenants including a maximum allowable debt:EBITDA leverage ratio and minimum required EBITDA:interest coverage ratio. The Partnership remained in compliance with all covenants at June 30, 2011 and throughout the period.

The fair value of long-term debt at June 30, 2011 was $114.6 million (US$118.8 million).

10. Related Party Transactions

The Partnership's transactions with related parties are consistent with the transactions described in the December 31, 2010 audited consolidated financial statements and are based on agreed upon amounts between the parties, and are summarized below:

(millions of dollars, unaudited)	Three months ended June 30, 2011	June 30, 2010	Six months ended June 30, 2011	June 30, 2010
Transactions				
Canfor – purchase of wood chips and other	**27.2**	35.5	**56.2**	69.7
CPPI administrative cost recovery	**0.1**	-	**1.0**	-
Howe Sound LP – commission	**-**	0.6	**-**	1.2
Lakeland Mills Ltd. – purchase of wood chips	**2.8**	1.5	**6.2**	2.7

	June 30, 2011	December 31, 2010
Balance Sheet		
Included in accounts payable and accrued liabilities:		
Canfor	**44.1**	44.5
Lakeland Mills Ltd.	**0.6**	0.4
Included in other accounts receivable:		
CPPI	**1.0**	-
Included in trade accounts receivable:		
Product marketed for Canfor	**30.7**	23.2

Transactions and payables to Canfor include purchases of wood chips, pulp and administrative services.

11. Derivative Financial Instruments

The Partnership uses derivative instruments to reduce its exposure to risks associated with fluctuations in foreign exchange rates, pulp and natural gas prices.

For the second quarter of 2011 the Partnership recorded a net gain on derivative financial instruments of $1.0 million (second quarter 2010 – net loss of $3.8 million) relating to the settlement of maturing contracts during the quarter, and the revaluation to market value of outstanding contracts at the end of the quarter, for natural gas swaps and US dollar forward contracts.

The Partnership recorded losses of $0.6 million during the second quarter of 2011 (second quarter 2010 – $0.8 million) relating to settlement of maturing natural gas contracts as a charge to non-operating income. At June 30, 2011 the Partnership had outstanding commodity swaps hedging future natural gas purchases of 0.2 million gigajoules extending to October 2011. At June 30, 2011 the unrealized loss of $0.8 million (June 30, 2010 – loss of $3.7 million) on these outstanding commodity swaps was recorded as a liability in accounts payable and accrued liabilities and in long-term liabilities.

The Partnership recorded a gain of $0.2 million during the second quarter of 2011 (second quarter 2010 –$0.3 million) on settlement of maturing US dollar forward contracts as a charge to non-operating income. At June 30, 2011 the Partnership had outstanding US dollar forward contracts of $78.5 million extending to October 2011. At June 30, 2011 the unrealized gain of $1.2 million (June 30, 2010 –loss of $3.3 million) on these outstanding US dollar forward contracts was recorded as an asset in other accounts receivable.

12. Distributions

The Partnership declared distributions in the first six months of 2011 as follows:

(millions of dollars, except per unit amounts, unaudited)

Record Date	Payable Date	Amount per Partnership Unit $	Amount $
January 31, 2011	February 15, 2011	0.26	**18.5**
February 28, 2011	March 15, 2011	0.26	**18.6**
March 31, 2011	April 15, 2011	0.26	**18.5**
April 29, 2011	May 13, 2011	0.23	**16.4**
May 31, 2011	June 15, 2011	0.23	**16.4**
June 30, 2011	July 15, 2011	0.23	**16.4**
		1.47	**104.8**

13. Green Transformation Program

The Partnership has been allocated $122.2 million under the Canadian Federal Government Pulp and Paper Green Transformation Program (the Program). The Program is designed as a reimbursement of funds to be spent on qualifying energy and environmental capital projects. Credits may be used until the Program end date of March 31, 2012. The Partnership has received Program approval to proceed with four projects totaling $157.4 million of which $122.2 million will be reimbursed under the Program. As of June 30, 2011 the Partnership has incurred $79.0 million and received reimbursements totaling $51.4 million with the balance of $27.6 million receivable as at June 30, 2011. The Partnership submits claims for expenditures on approved projects under the Program on a monthly basis. These projects are expected to provide economic and environmental benefits to the Partnership's operations.

14. Segmented Information [a]

The Partnership is a producer of market NBSK Pulp and fully bleached, high performance Kraft Paper. For management purposes, the Partnership has two reporting segments which operate as separate business units: Pulp and Paper. These divisions are the basis on which the Partnership reports its primary segment information. This segment reporting is consistent with the internal reporting provided to the executive management team, who operate as the Partnership's chief operating decision maker. The executive management team is responsible for allocating resources and assessing performance of the operating segments.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

The Partnership accounts for intersegment sales and transfers as if the sales or transfers were to third parties, that is, at current market prices. All such sales and transfers are eliminated on consolidation.

(millions of dollars, unaudited)	**Pulp**	**Paper**	**Unallocated**	**Total**
Three months ended June 30, 2011				
Sales to external customers [b]	**207.5**	**34.2**	**0.4**	**242.1**
Sales of pulp to paper segment [c]	**21.6**	**(21.6)**	**-**	**-**
Operating income (loss)	**52.0**	**0.7**	**(3.6)**	**49.1**
Amortization	**14.1**	**0.9**	**-**	**15.0**
Capital expenditures, net	**7.1**	**1.0**	**0.5**	**8.6**
Three months ended June 30, 2010				
Sales to external customers [b]	214.8	32.5	0.3	247.6
Sales of pulp to paper segment [c]	24.2	(24.2)	-	-
Operating income (loss)	56.9	(0.5)	(4.3)	52.1
Amortization	16.3	0.9	-	17.2
Capital expenditures, net	7.5	0.4	0.3	8.2
Six months ended June 30, 2011				
Sales to external customers [b]	**424.8**	**68.2**	**1.4**	**494.4**
Sales of pulp to paper segment [c]	**44.1**	**(44.1)**	**-**	**-**
Operating income (loss)	**102.8**	**2.7**	**(6.5)**	**99.0**
Amortization	**29.7**	**1.7**	**0.1**	**31.5**
Capital expenditures, net	**11.4**	**1.8**	**1.1**	**14.3**
Identifiable assets	**715.7**	**65.0**	**42.8**	**823.5**
Six months ended June 30, 2010				
Sales to external customers [b]	419.6	67.0	0.5	487.1
Sales of pulp to paper segment [c]	42.9	(42.9)	-	-
Operating income (loss)	94.4	(1.0)	(8.3)	85.1
Amortization	31.7	1.7	0.1	33.5
Capital expenditures, net	14.8	0.8	0.5	16.1
Identifiable assets	747.8	64.8	57.1	869.7

(a) Operations are presented by product lines. Operations are considered to be in one geographic area since all production facilities are in Canada. Substantially all sales are exported outside Canada, with sales to the United States representing 28% (Year 2010 – 37%).

(b) Sales to the largest customer represented approximately 8% of pulp segment sales (Year 2010 – 12%).

(c) Sales of slush pulp to the paper segment are accounted for at approximate market value. The sales are transacted as a cost transfer and are not reflected in Pulp sales.