REMARKS BY HANK KETCHAM

TO COFI CONVENTION

April 12, 2007

I have been asked to speak on the topic of "Competitiveness – The Necessary Ingredients". Given the state of the industry today, this is definitely a timely subject.

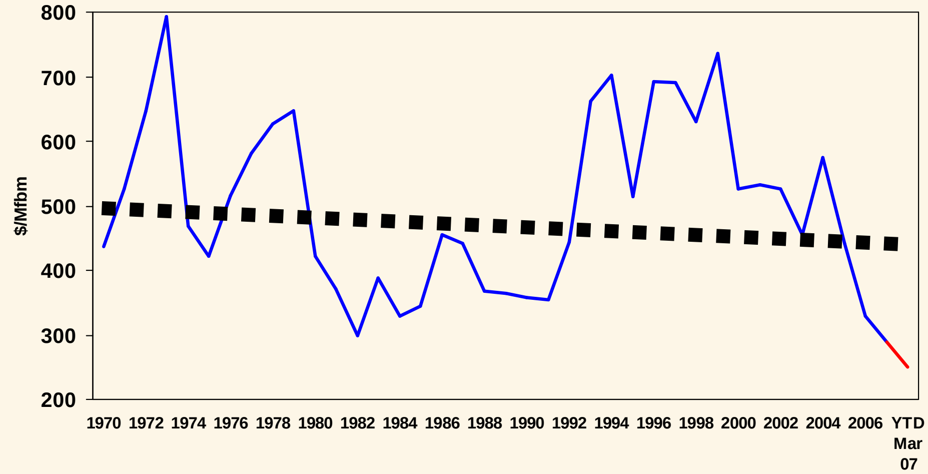
The problem is B.C.'s Interior lumber industry has written the book on competitiveness over the past several decades leaving little for me to say that you don't already know.

The mill owners and operators that are in the audience today have arguably created the most competitive lumber industry in the world.

To a large extent, we owe our success to the generation that came before us – the entrepreneurs who often risked personal bankruptcy to sow the seeds of the industry we have today. This industry grew up not to supply chips to large capital intensive pulp mills but rather to make money the old fashioned way – by making lumber. The pulp mills came later. The result was a sawmill industry that learned how to spend money wisely and that knew that its very survival depended on continual cost reduction – a concept not so clearly grasped by the emerging pulp industry.

Inflation Adjusted Lumber Price

2006 Dollars - CDN $ 2x4 Std&Btr



2 Source: RISI

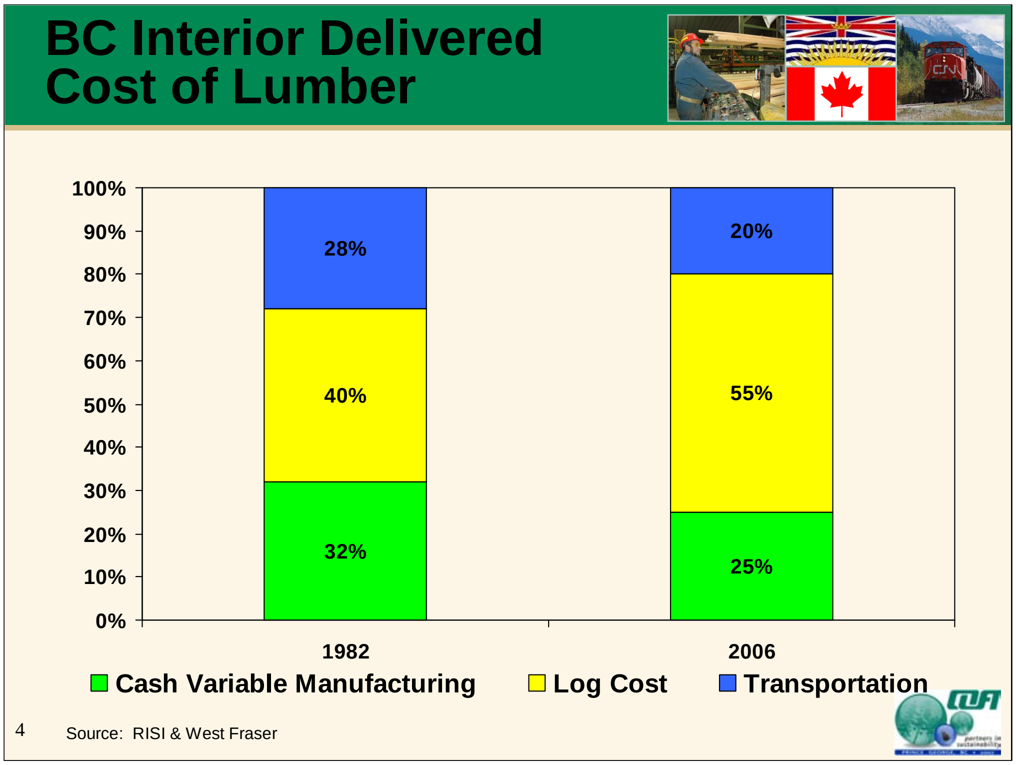
A look at this graph tells us all we need to know about the necessity of relentlessly pursuing cost reduction in our lumber operations. Those of us who have been in the business since the early seventies have a long experience in the boom and bust cycles of the industry. We suffered through severe lumber depressions in the mid 70's, the early 80's and the early 90's. And of course, we could be facing the worst lumber price depression of all if the current housing bust in the U.S. continues much longer.

The bottom line is that the long term survivors in this business realize that peak prices always lead to trough prices and the troughs are brutal. As you can see, today's Canadian $ denominated price of lumber in real terms, is lower that it was in 1982.

So how do we manage our business in such a volatile and unpredictable environment? The great operators in the room today have learned that cost reduction – attained primarily through increased lumber production and lumber recovery, is the way to survive the downturns and prosper when things improve.

But the lumber companies do not bear all the responsibility for ensuring the ongoing competitiveness of our interior industry. In fact, we are in a three way partnership in competitiveness. This partnership involves:

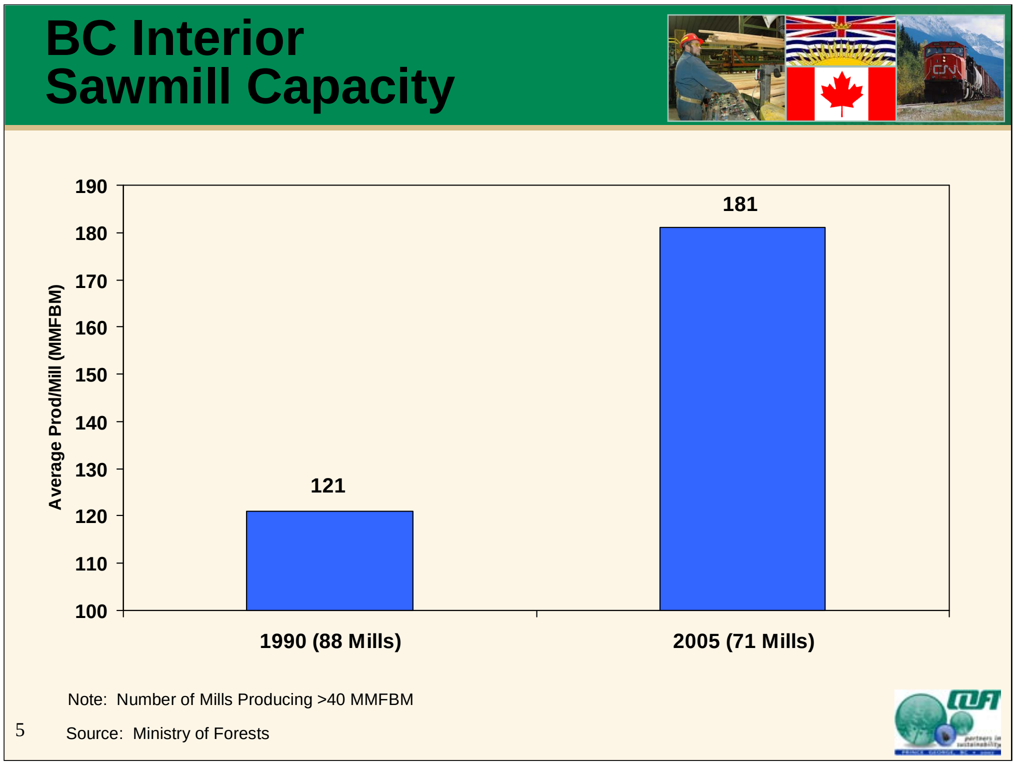
- Industry
- Government
- Railroads



This slide represents the three components of the delivered cost of lumber and compares the relative change in key cost components between 1982 – our previous worst lumber market – and 2006, the beginning of perhaps the most severe pricing downturn in memory.

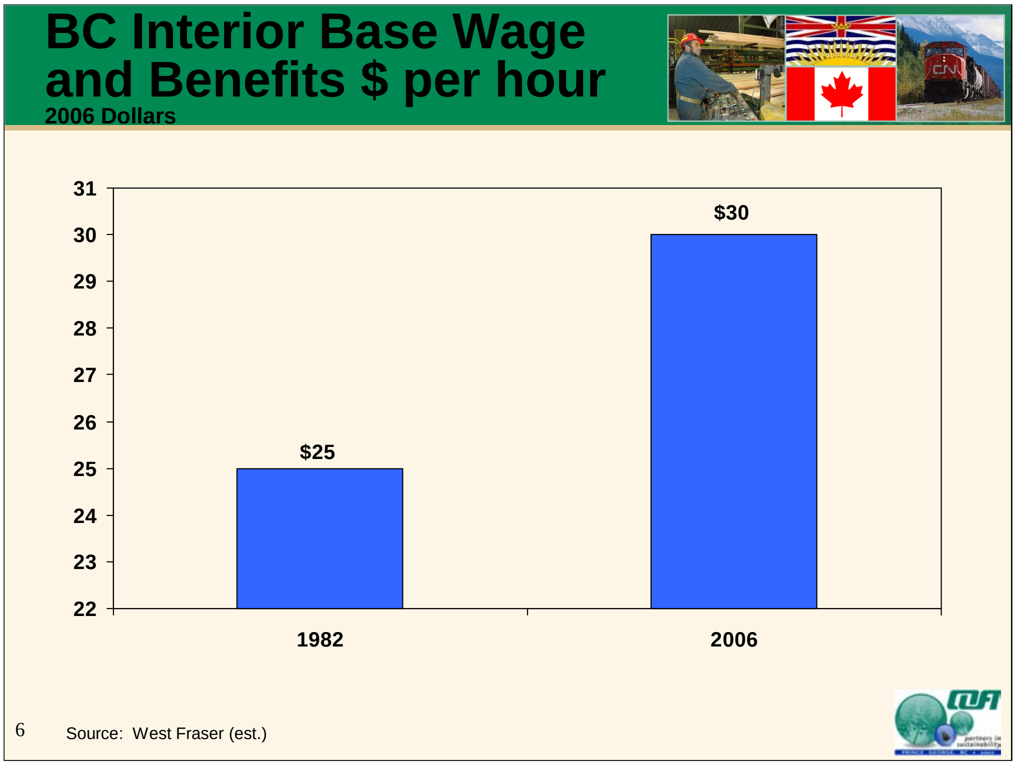
In simple terms, both the lumber and rail sectors have reduced their share of costs while the Provincial Government has significantly increased its proportion of delivered costs.

Let's first look at what the lumber industry has done to reduce costs and improve its competitiveness.



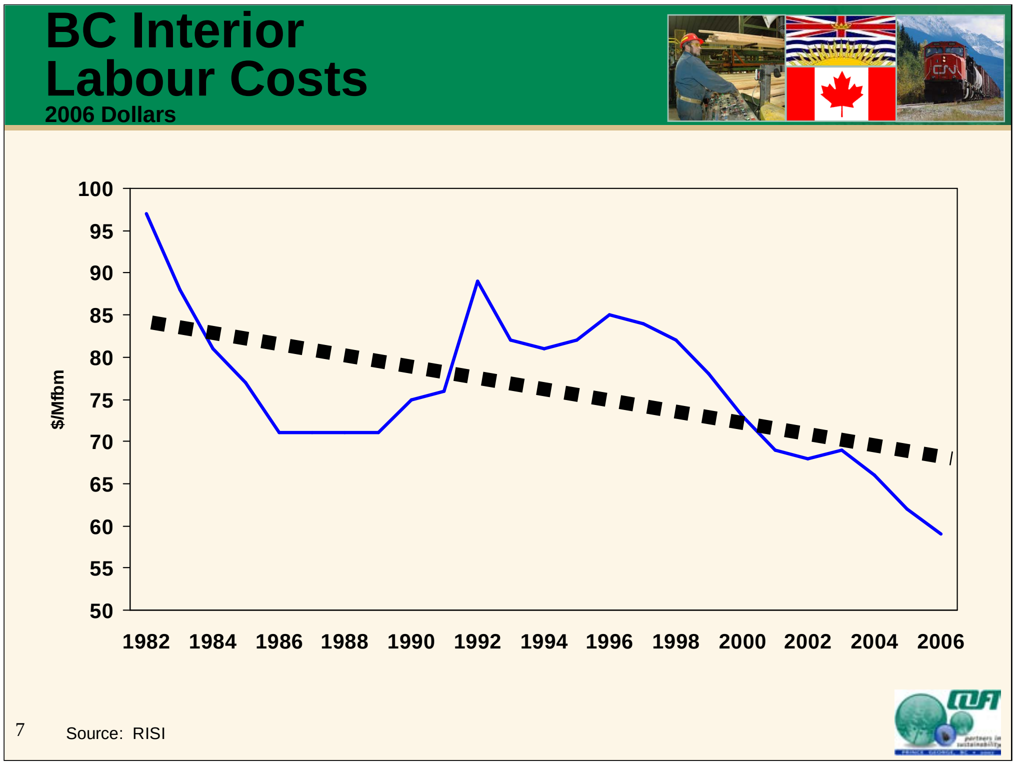
As you can see, there were 88 lumber mills in the B.C. Interior in 1990 producing an average of 121 MMfbm per mill.

Today 71 mills produce an average of 181 MMfbm per mill. Obviously, the increased Beetle harvest skews these numbers beyond what they would have been but the trend to consolidate and improve throughput to reduce costs is clearly there.



One of the largest non-wood components of our cost structure is labour costs.

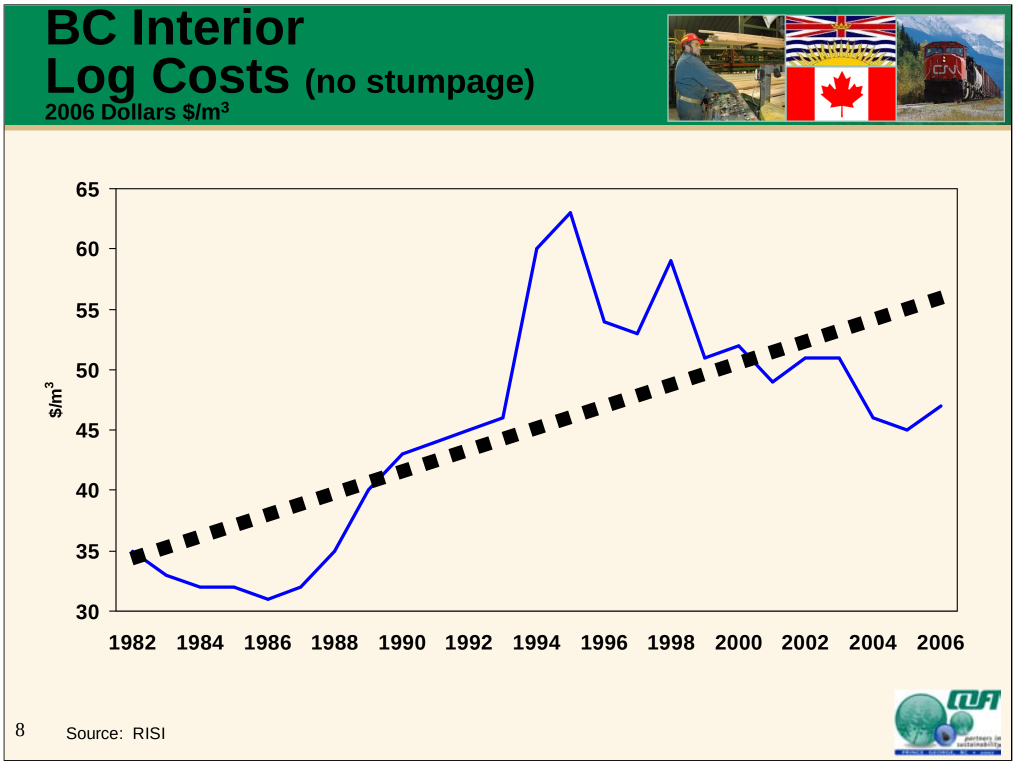
Wages and Benefits have risen, in inflation adjusted dollars, from $25 per hour in 1982 to $30 per hour in 2006. I've shown the wage difference in real dollars to show the significant increase in real earnings for forest sector employees.



But when calculated on a per MFBM basis, we have driven real dollar wage costs down by 19% since 1982.

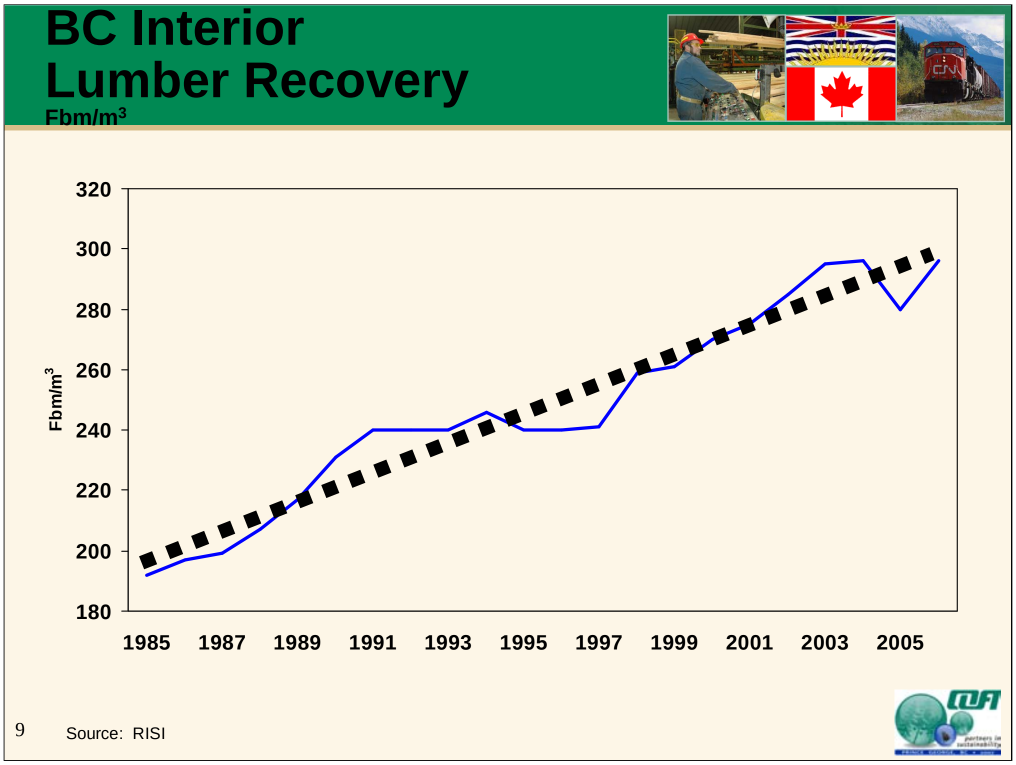
Again, this has been achieved through technology and capital investment while continuing to ensure our employees have a wage and benefits package that is among the best industrial packages in Canada.

But remember, in an industry that has seen no real increase in pricing in twenty five years, we must continue to find ways to offset each dollar increase in wage costs with a corresponding increase in productivity.



Another big cost component, log costs, have increased significantly over the years. This is primarily due to an off-loading of tenure obligation costs by Government and more stringent forest practice standards since the mid 90's.

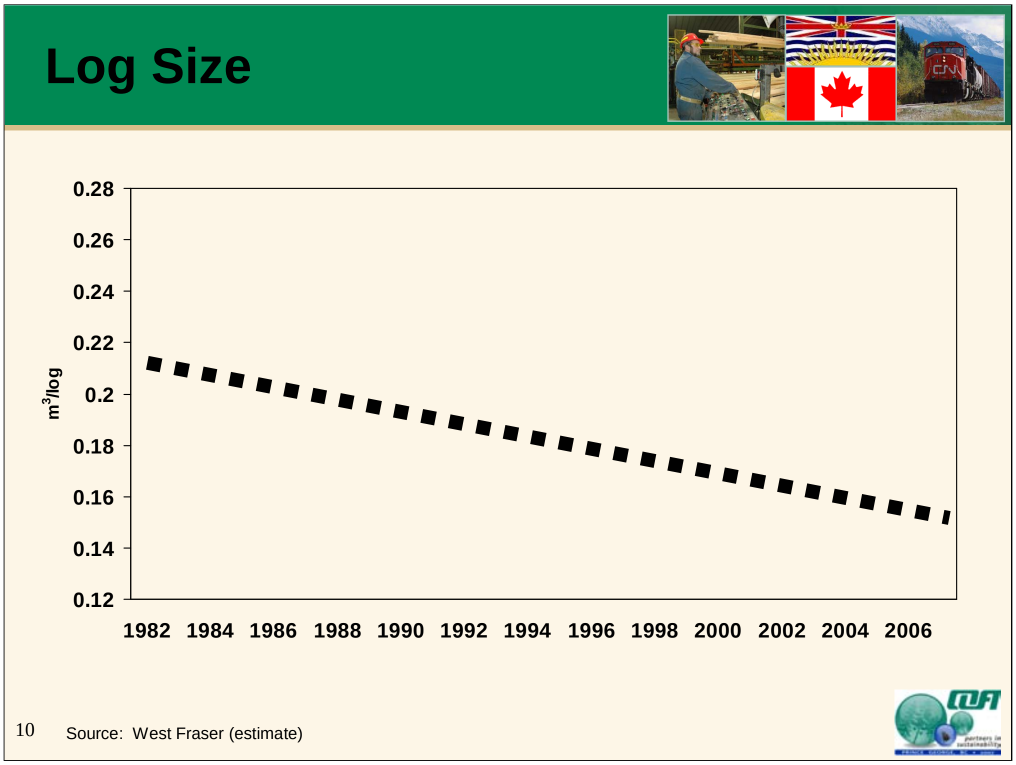
I would be remiss if I didn't acknowledge the tremendous efforts our independent logging and trucking contractors have made over the years to improve their productivity as well. They have made significant investments in equipment and technology to control their costs and improve the quality of logs delivered to our mills.



To deal with rising wood costs, the industry has invested hundreds of millions of dollars to install equipment and technology to improve the yield we get out of each log harvested.

Today we recover about 50% more lumber from each log than we did in 1985.

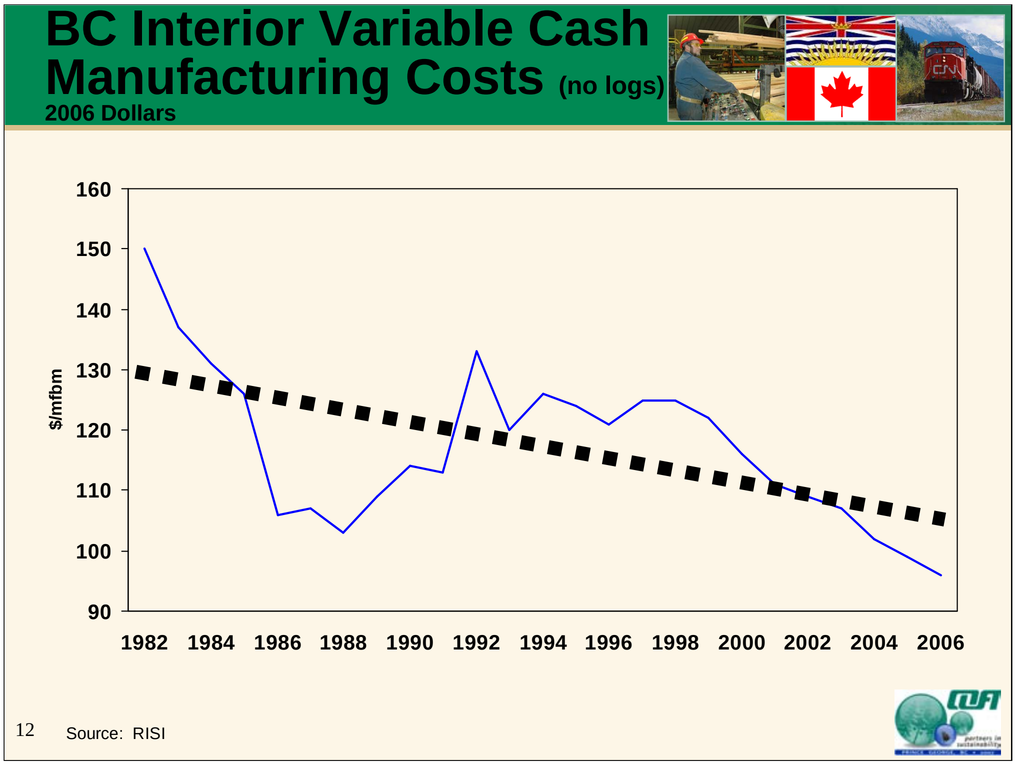
As a result, while log costs per M3 have increased about 30% in real terms since 1982, log costs per MFBM have increased by only 3%.



And what all of the mill operators in the room know is that during this period, the average log size has declined steadily.

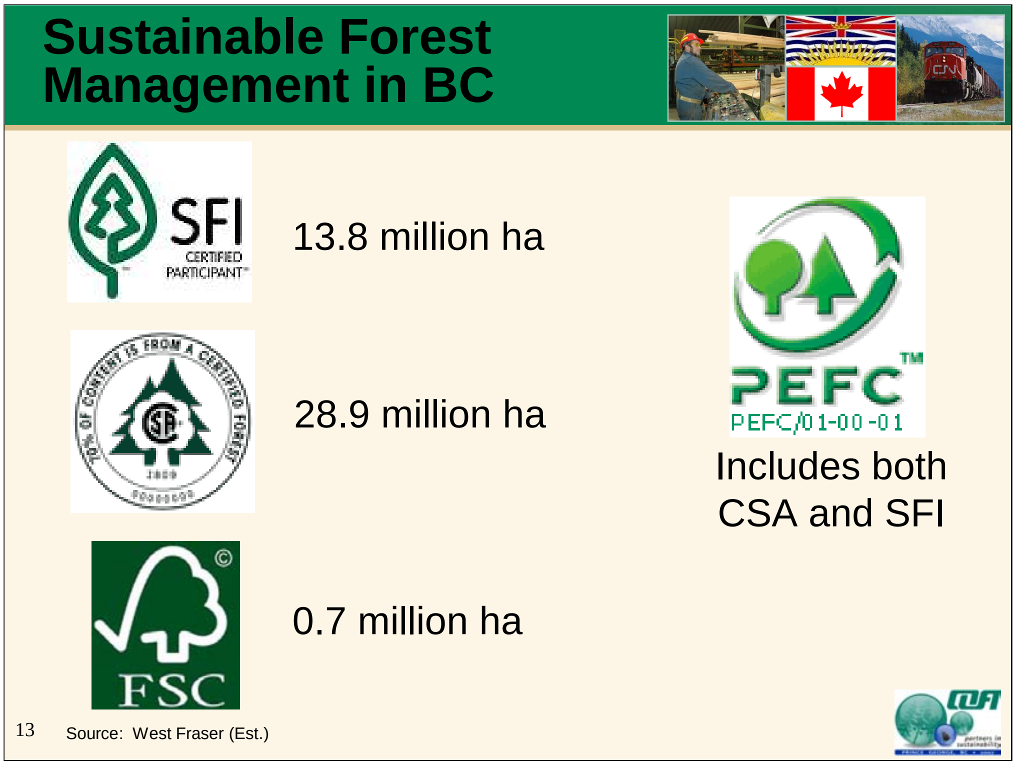
This slide shows the trend in one of our typical Interior mills over the past 25 years.

Not only has log size declined but log quality, particularly with respect to Beetle attacked timber, has declined substantially as well.



So in the face of increasing costs for labour, energy and other inputs, and a declining log size, I believe this slide tells a great story for our industry and reflects on the ingenuity and competitive spirit of many of you in the audience.

As a result of huge capital investments, we have actually reduced our real variable manufacturing costs by 15% since 1982.



In addition to reducing our controllable costs, we have made great strides in continuing to reduce our impact on the environment. The public and our customers want wood products from sustainably managed forests. Today, the large majority of the timber harvested in the B.C. Interior is third party certified to strict sustainability standards.

Our industry and our Provincial Government have shown leadership in this area and I know that just as we have continued to respond to the cost pressures facing us, we will also continue to be world class leaders in proactively reducing our industry's environmental footprint.

I said at the outset that the competitivess of the Interior lumber sector relies on a 3 way partnership. The second partner is Government, both Provincial and Federal.

Let's start with the Provincial Government.

Since it controls 100% of our raw material supply, the province has a responsibility not only to our industry, but to our employees, contractors and our communities to ensure that we have a secure and affordable log supply. Without this, investors will look elsewhere and our industry will decline no matter how productive we are.

The Province, led by Gordon Campbell, has made a number of policy changes in recent years which will help to improve competitiveness such as the changes to appurtenancy and cut control regulations.

But in a world of declining real prices for the products we produce – lumber and pulp - our provincial Government needs to be just as focused on the cost of logs to our mills as we are. This means resisting the urge to add regulatory cost and ensuring that the price charged for the Province's timber truly reflects its value.

On this point, there is no better example than the Mountain Pine Beetle infested timber most of us are dealing with in our mills today.

Our beetle killed pine stands have deteriorated significantly in the last year and in many cases can no longer be economically salvaged given today's costs.

The Province must ensure that the stumpage appraisal process which prices this timber is up to date and reflects current costs and product values. As well our scaling system must only designate as sawlogs those logs that will truly yield merchantable lumber.

Waste?

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As these beetle killed stands continue to deteriorate, more and more of the trees do not meet the sawlog test and without an alternate use, must be left behind as waste.

As industry we recognize the public concern that this situation has raised and we are working hard on alternative uses for this material including bio-energy.

In the meantime, the Province should not move to penalize the industry for leaving this material behind as this would simply create a huge disincentive to the aggressive salvage program under way today.

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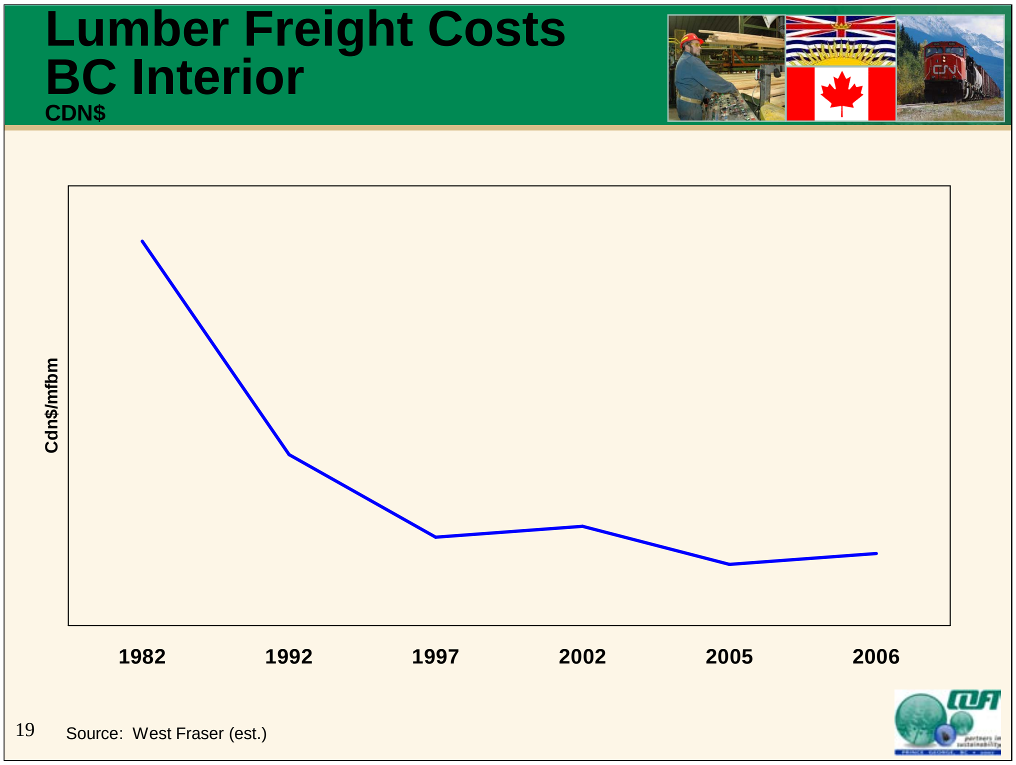
The Federal Government is another partner in competitiveness. It has jurisdiction in areas such as taxation, international trade and mergers and acquisitions just to name a few.

On the international trade front, we are all familiar with the agonizing process we went through to settle the softwood lumber dispute. I'm sure we all have our own opinions as to whether or not we negotiated the best possible deal for our country.

The agreement includes a variety of untested rules. Several key issues were left open when the agreement was struck with the intention that these issues would be settled by further negotiation or through binational panels. It is imperative that our government aggressively defend our rights under this agreement and not allow the U.S. industry to use the SLA to inhibit our efforts to improve our competitiveness.

Finally, the Federal Competition Bureau oversees mergers and acquisition in Canada. Today, Canada's largest forest company is small by international standards. It is time to review the rules under which the Bureau operates in order to facilitate the continued growth of a strong world class industry.

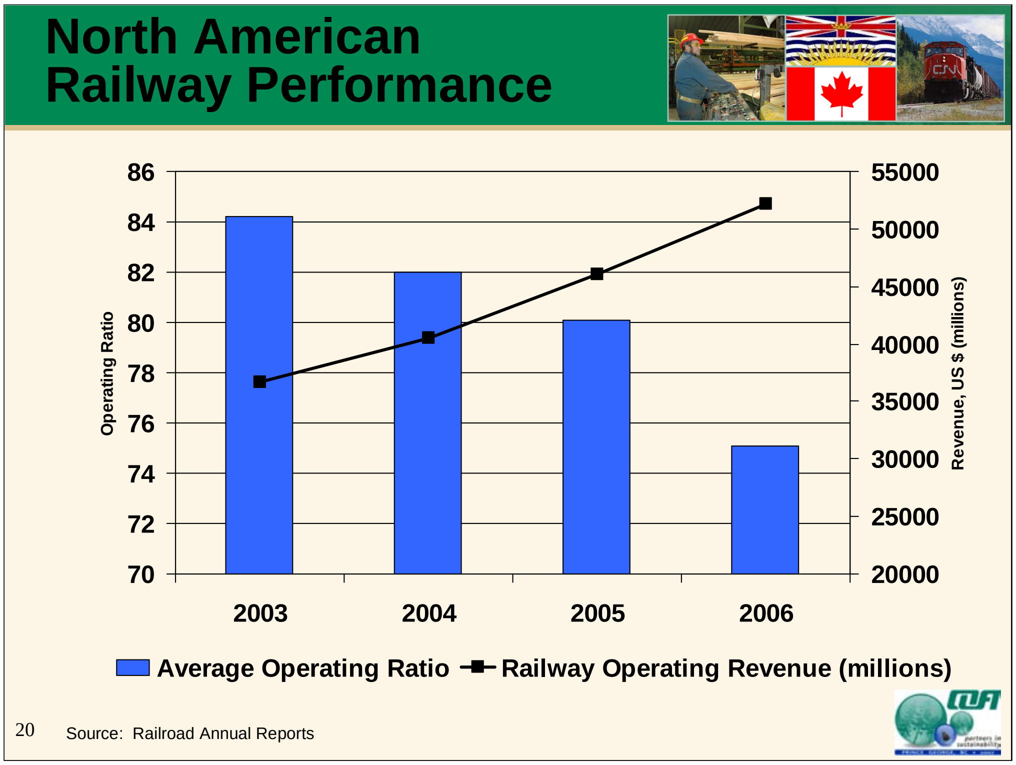


The third partner in competitiveness is the transportation industry, particularly the railways. Over 80% of BC Interior lumber shipments go to U.S. or Eastern Canadian destinations by rail. Freight is our second largest cost component after logs. Competitive freight costs are critical to the BC Interior.

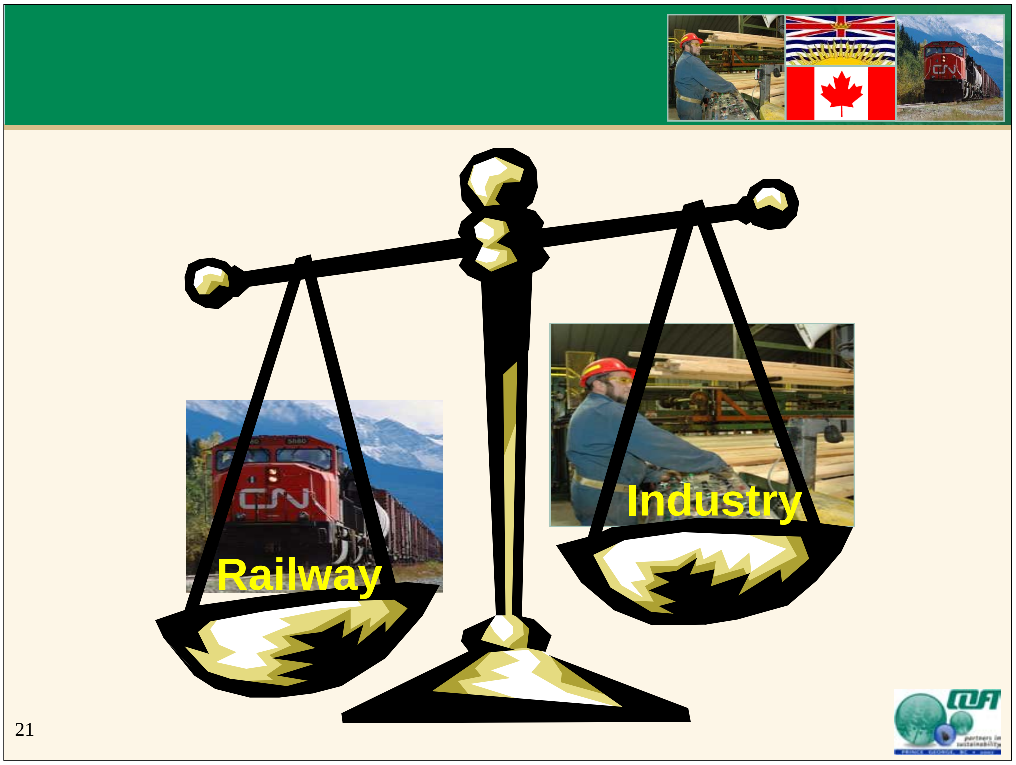
This slide, showing freight costs in real $Cdn/mfbm, indicates that the railways have done a good job over the years. Following U.S. deregulation in 1980, productivity improvements drove rail costs, and prices, down. There is a good example in the lumber industry - in 1982 the standard rail shipment was about 65 mfbm on a 52' BH flat. Today it is about 110 mfbm on a 72' CB - nearly a 70% productivity gain. Railways have been among the leaders in industrial productivity improvements over the past 25 years.

Since 1997 however, actual freight costs have been increasing consistently, along with railway productivity. As a result productivity sharing has ceased, or at least slowed down. Today, freight costs are about 20% of our delivered price and have reached the point again where carriers are taking a larger piece of the pie than would be expected in a competitive environment.

Freight rates are not the only issue.



This chart compares total revenues to a standard measure of railway productivity - operating ratio – which is the percent of revenue consumed by railway operations. Despite coping with rapid growth, the railways have managed to improve operating efficiency. However, this improvement has not been reflected in car supply and local service, at least in the B.C. Interior. The result is idle car loading crews, overtime and weekend work to catch up, car demurrage bills, large inventories, missed or late shipments, or buying premium alternative services. All this causes higher delivered costs not captured in the rate analysis.



So, why does the relationship with such a significant business partner seem so difficult? I think it is a matter of unequal market power. As BC Interior shippers, we have little or no effective competitive alternative.

This imbalance needs to be addressed. We don't want a regulated transportation industry. Nor do we want third parties to resolve our issues. But we do need some improved leverage in our discussions with the railways. Modest changes to the CTA that make access to third party arbitration simpler, quicker and cheaper are required – including joint application on issues of general or common interest.

These stronger shipper oriented regulations are needed to create a more balanced and meaningful negotiating environment between the railways and their shippers.

So in conclusion, I believe each of the partners in competitiveness have contributed to building a world leading industry of which our host communities here in the Interior should be justly proud. Our companies have invested hundreds of millions of dollars to become the most competitive producers in the world. In so doing, we have encouraged the development and growth of equipment and technology companies that are leaders in their fields and export their equipment and expertise around the world. Combine that with our great forestry schools at UNBC and UBC and, hopefully, a reinvigorated forest technician program at BCIT and we have clearly created a world leading Centre of Excellence in lumber manufacturing right here in B.C.

In recent years, our Provincial Government has worked hard to understand our industry and break down many of the impediments to improved competitiveness in our sector. I can personally attest to the active and forceful role our Premier played in protecting and promoting B.C.'s interests in the recent softwood lumber dispute. But because the B.C. Government holds so many of the cards in respect of our ability to effectively compete in the future - I urge our Provincial leaders to actively engage industry in discussions that will improve our competitiveness while giving a fair return to the Province.

And finally, we are fortunate to be served by one of the most efficient railroads on the continent. But a virtual monopoly brings with it, I believe, an obligation to treat the customer as though that customer had alternatives. In the absence of this, Government must step in to balance the playing field.

I am sorry to have gone on so long but hope I have painted a picture of optimism in what is clearly a very dark period for our industry. The entrepreneurs and mill personnel in this room today are world leaders in ingenuity, risk taking and competitiveness. You have proven time and time again that you can survive the tough times and emerge even stronger when the market improves.

What I find most exciting is that after fifty years of building this industry in the Interior, we are still approaching the many new challenges coming our way with the same practical, common sense, can-do attitude that has been the hallmark of this industry since its inception. In fact, challenge and adversity fuels the competitive spirit that drives innovation and efficiency. We have proven that no one responds to these challenges better than the Interior lumber industry right here in the heart of British Columbia.

Thank you.