



The following discussion and analysis should be read in conjunction with the consolidated financial statements and notes thereto included in this Annual Report.

**Lumber**

**Table A**

	2003	2002
Production — SPF — MMfbm	2,295	2,064
Production — SYP — MMfbm	299	283
Shipments — SPF — MMfbm	2,312	2,014
Shipments — SYP — MMfbm	305	283
Chip Production — softwood oven dried Mtonnes	1,075	1,013
— SYP oven dried Mtonnes	165	144
Net sales — \$millions	861	931
EBITDA — \$millions	99	194
EBITDA margin — %	11	20
Operating Earnings — \$millions	40	139
Capital Expenditures & Acquisitions — \$millions	62	84
Benchmark Price		
— SPF #2 & Better 2 x 4 — (per Mfbm) <sup>1+2</sup>	US\$ 277	US\$ 270
— SYP #2 West 2 x 4 — (per Mfbm) <sup>1</sup>	US\$ 331	US\$ 302

1. Source: Random Lengths—price before duties  
2. Gross price before duties

**LUMBER**

Although shipments increased by 14% over the previous year and SPF and SYP benchmark prices were both higher, net sales, EBITDA and operating earnings in West Fraser's lumber segment were substantially lower than in 2002. The decrease was due primarily to the stronger Canadian dollar and to the payment of higher softwood lumber duties for the full year compared to approximately seven months in the previous year.

Production increased over the previous year by 11%, with production and efficiency records set at several of the Canadian mills. This was due to

continuing capital expenditures on projects that increase lumber recovery and enable productivity improvements and to the dedicated efforts of the employees to maximize production at the plants. Also, additional shifts were added in some operations to process logs that became available due to the extensive pine-beetle infestation in British Columbia.

Sales prices were low during the first half of the year due to an oversupply of lumber. Several large forest fires and announcements of some mill curtailments caused the market to rally during the summer. Prices remained higher for the last half of the year, driven by continued strong U.S. housing starts and renovation activity.

In British Columbia and Alberta, West Fraser consumes approximately the same volume of chips as it produces. Prices for softwood chips in western Canada, which are based primarily on the price of market pulp, remained near 2002 levels. For the U.S. South mills, prices for SYP chips, based on the market for pulpwood in the region where produced, were also similar to those in 2002.

The U.S. softwood lumber duties, as shown in Table B, significantly reduced West Fraser's financial results. For further detail on this matter see "Risks and Uncertainties - U.S. Trade Dispute."

The Terrace sawmill suspended production on May 28, 2003, as the labour disruption at the Kitimat linerboard and kraft paper mill closed its primary market for by-product chips. The strike also caused the Smithers mill and the joint venture mills at Houston and Burns Lake to stockpile chips, although they continued to produce lumber. The strike ended in September 2003, but Terrace remained closed until early February 2004 as there was an oversupply of chips in the region. This event reduced lumber production by approximately 50 MMfbm in 2003.

The Seehta joint venture operation at Red Earth, Alberta remained unprofitable due to low lumber prices, the strong Canadian dollar and the low grade of lumber recovered from poor quality burned

**Export Duties (\$ millions)**

**Table B**

	Q1	Q2	Q3	Q4	Total
2003 Charge	\$ (23.3)	\$ (26.3)	\$ (30.7)	\$ (31.7)	\$ (112.0)
2002 Charge	\$ (3.7)	\$ (10.2)	\$ (28.9)	\$ (24.6)	\$ (67.4)
2002 Reversal of 2001 Charge	2.0	23.0	—	—	25.0
Total for 2002:	\$ (1.7)	\$ 12.8	\$ (28.9)	\$ (24.6)	\$ (42.4)



### Blue Ridge Sawmill



(L to R) Scott Steinke, sawfiler, Mac Gavin, sawfiler

### Skeena Sawmill



Manuel Cordeiro, bin attendant, planer mill

wood processed during the year. Presently, West Fraser is financing the operation's working capital requirements.

West Fraser continues to be committed to improving productivity at its U.S. South operations, and has recently increased the presence of senior management. The rebuild of the Huttig, Arkansas mill, deferred from 2002 because of permitting delays, began in 2003. There were several weather-related delays, and completion is now expected in the first quarter 2004, making both the Huttig and Joyce sawmills among the most modern and efficient in the industry.

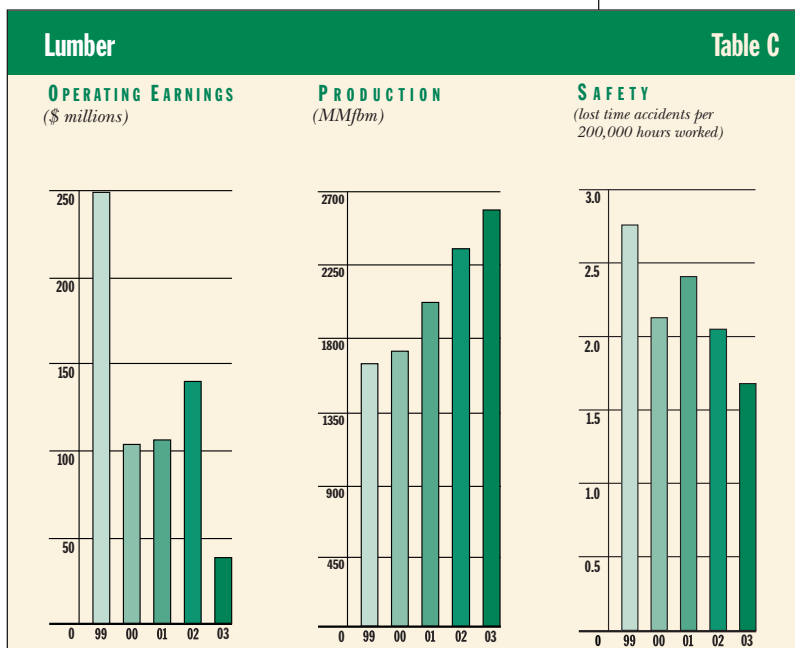
West Fraser plans to spend more than \$100 million on capital improvements to its lumber

operations in 2004, the largest single-year mill improvement program in its history. Most of the projects are high pay-back and are expected to begin to show results in 2005.

During 2002, the government of British Columbia introduced a new results-based *Forest and Range Practices Act* to replace the highly prescriptive and rigid *Forest Practices Code of British Columbia Act*. At the end of January 2004, this legislation took effect and it will tighten accountability, expand the requirements for security deposits and significantly increase penalties for non-compliance. West Fraser expects that new regulations related to the legislation will be fully implemented by the end of 2004, and will

allow more flexible and efficient forest management without sacrificing existing high environmental standards.

Under the Forestry Revitalization Plan ("FRP") introduced in March 2003, the government of British Columbia, subject to certain exceptions, reduced the AAC allocated to holders of long-term forest tenures by 20%. It is intended that the timber volumes that this will make available will be used by the Ministry of Forests to implement



an auction-based timber pricing system as well as to address First Nations claims and certain community concerns. The take-back from West Fraser was approximately 832,000 m<sup>3</sup>. Since most of the timber from the areas withdrawn is expected to be available for purchase on the open market, West Fraser believes that, as a low-cost producer, it will continue to be able to obtain sufficient fibre for its mills. Legislation provides for compensation to licensees for the reduction in AAC and for related costs that have been incurred for roads and bridges. The amount of compensation has not been determined.

The proposed reform to the provincial timber pricing policy is a key component of the FRP. It proposes that stumpage will no longer be determined administratively, but will be based on public timber auction prices. Market-based pricing on the B.C. coast is expected to be effective February 29, 2004 and may be implemented in the interior region by the end of the year, although the timing and pricing specifics are unclear at this time.

2003 was one of the worst years for wildfires in British Columbia's history. The fires were mostly confined to the southern regions of the province, with only minor incursions into West Fraser's timber harvesting areas.

In British Columbia's central interior, a mountain pine beetle infestation has been spreading since 1994. During the last several years, both the rate of spread and the intensity of the attack have increased exponentially. Recent timber supply analyses indicate that, unless the infestation collapses, the availability of timber in the long term will be affected. While the epidemic will not compromise the productive capability of the land, the medium-term timber supply reduction could range from 10% to 30% of pre-epidemic levels. In the short term, however, AAC levels throughout the central interior have been increased by 6.8 million cubic metres and they are likely to be further increased. With the exception of Terrace and Chetwynd, all West Fraser sawmills in British Columbia are processing logs primarily from beetle-damaged stands.

Unsettled claims of First Nations groups may also affect West Fraser. This is discussed separately

under "Risks and Uncertainties – First Nations Claims".

The outlook for lumber prices in 2004 is largely dependent on continued low interest rates and strong housing starts in the U.S. Also, uncertainty regarding a possible resolution of the softwood lumber dispute will continue to create volatility in the markets. In the absence of the imposition of a quota, lumber production in 2004 is expected to increase approximately 10% over 2003 levels. For further detail on this matter see "Risks and Uncertainties – U.S. Trade Dispute."

## PANELS

Net sales, EBITDA and operating earnings were lower in 2003 than in the previous year, mostly the result of the decline in revenues due to a less desirable product mix in MDF and the stronger Canadian dollar.

## MDF

In 2003 Ranger Board set a production record 8% above its previous best. WestPine, although shut down for 16 days in April for major maintenance, exceeded its 2002 production levels. Capital expenditures planned for 2004 will further optimize production at both plants.

Natural gas is an energy source and a major component in the resin used in manufacturing MDF. A substantial increase in the price of natural gas during the year was a major factor in higher

Panels	Table D	
	2003	2002
Production — MDF — Mmsf — 3/4" basis	261	249
Shipments — MDF — Mmsf — 3/4" basis	263	249
Production — Plywood — Mmsf — 3/8" basis	248	235
Shipments — Plywood — Mmsf — 3/8" basis	237	235
Net sales — \$millions	199	217
EBITDA — \$millions	37	70
EBITDA margin — %	19	32
Operating Earnings — \$millions	13	47
Capital Expenditures — \$millions	5	12
Benchmark Price — MDF (3/4" basis per Msf) <sup>1</sup>	US\$ 375	US\$ 405
— Plywood (3/8" basis per Msf) <sup>2</sup>	C\$ 442	C\$ 405

1. Source: RISI and West Fraser database

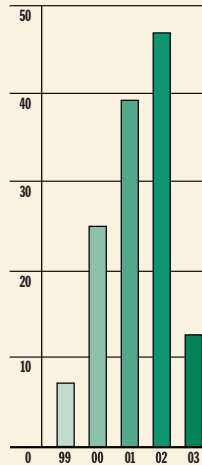
2. Source: Crow's



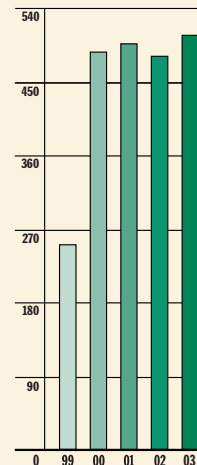
**Panels**

**Table E**

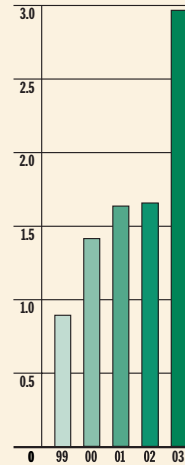
**OPERATING EARNINGS**  
(\$ millions)



**PRODUCTION**  
(MMsf)



**SAFETY**  
(lost time accidents per 200,000 hours worked)



manufacturing costs at both mills.

MDF markets have changed significantly in recent years. The U.S. furniture manufacturing industry, an important market for MDF, is being threatened by offshore imports. As a result, West Fraser's exports of lower-value MDF to Asian markets were larger than planned, resulting in lower mill nets.

West Fraser is developing a customer base in the competitive market for the higher-value flooring and thinboard products that WestPine was designed to manufacture. To be recognized as a qualified supplier, a producer must meet demanding and

exact specifications. By the end of the year, West Fraser's efforts began to show results. Also, markets in general for composite panel products improved by year-end.

Faced with the high volume of furniture imports from overseas, North American MDF manufacturers are likely to continue to rationalize or consolidate, which should lead to improved pricing.

**PLYWOOD**

The plywood mill achieved record production in 2003. Prices were volatile, beginning the year quite low and declining further as bad weather continued into late spring, shortening the building season. However, a strong structural panel market caused prices to increase substantially in the summer and fall, reaching a historic high of Cdn\$ 606 per Msf, as listed in Crow's, a trade publication. They declined somewhat by December, a normal seasonal occurrence, but saw renewed strength by early 2004.

Market demand in Canada, where West Fraser sells most of its plywood, is expected to remain good in 2004. However, this is dependent on continued low interest rates, strong housing starts and renovation activity.

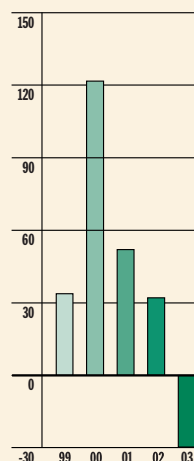
**PULP & PAPER**

The decreases in net sales, operating earnings and

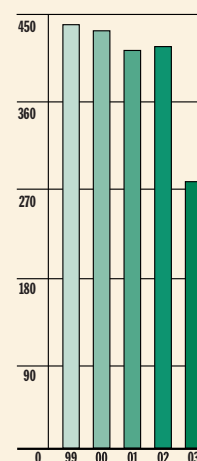
**Pulp & Paper**

**Table F**

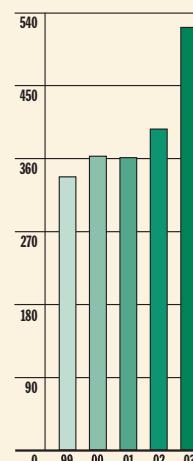
**OPERATING EARNINGS**  
(\$ millions)



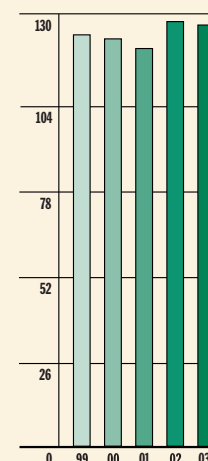
**LINERBOARD AND KRAFT PAPER PRODUCTION**  
(thousands of tonnes)



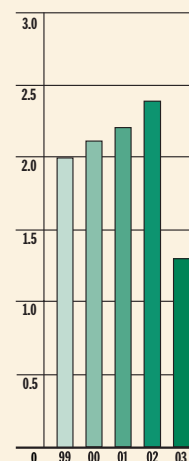
**PULP PRODUCTION**  
(thousands of tonnes)



**NEWSPRINT PRODUCTION**  
(thousands of tonnes)



**SAFETY**  
(lost time accidents per 200,000 hours worked)



EBITDA from the previous year were largely the result of a 110-day strike at the linerboard and kraft paper mill at Kitimat. In addition, the strengthening Canadian dollar reduced returns in all product lines.

## PULP

The 32% increase in pulp production was attributable largely to the November 1, 2002 acquisition of the other 50% of QRP. In addition, the Slave Lake Pulp mill set an annual production record for the fifth consecutive year.

QRP produces softwood BCTMP and TMP and small volumes of hardwood BCTMP. Production costs declined from the previous year despite higher prices for fibre and natural gas. The acquired capacity enabled the development of new grades for an expanded customer base. However, the trials associated with the grade development reduced production somewhat in the first half of the year. With the new capacity, West Fraser's production at QRP was increased by 63% from the previous year.

The Slave Lake Pulp mill produces mostly hardwood BCTMP, with a small volume of blended hardwood/softwood BCTMP. Since 1998, the capacity of this mill has increased by 57% as a result of capital spending and improved operating efficiencies. Total production costs rose slightly as a result of higher fibre costs and natural gas prices.

Demand for BCTMP increased, although at a slower rate in the second half of the year. Prices for both hardwood and softwood pulp improved, and although this was more than offset by the stronger Canadian dollar, both mills were profitable.

Prices for BCTMP are expected to remain at current levels through the first quarter of 2004, and show some improvement in the second quarter with expected increases in paper demand.

## LINERBOARD AND KRAFT PAPER

The 110-day strike, an extended annual maintenance shutdown and the stronger Canadian dollar made for a very poor year for the Kitimat mill.

The strike by members of the Communications, Energy and Paperworkers Union of Canada, Local 298 began on May 28, 2003 after contract negotiations failed. Employees returned to work on September 16.

The final agreement reached in September was very similar to the pattern agreement accepted by most of the bargaining units in British Columbia. The new collective agreement expires on April 30, 2008.

Despite disruption from the strike, operations at the mill improved. Importantly, the frequency of safety

## Pulp & Paper Table G

	2003	2002
Production — tonnes	929,906	935,547
Shipments — tonnes	929,206	912,644
Net sales — \$millions	449	485
EBITDA — \$millions	27	87
EBITDA margin — %	6	18
Operating Earnings — \$millions	(30)	32

## Pulp Table H

	2003	2002
Production — tonnes	523,027	396,957
Shipments — tonnes	512,492	385,638
Capital Expenditures — \$millions	8	10
Benchmark Price — BCTMP softwood pulp — (per tonne) <sup>1</sup>	US\$ 450	US\$ 392

1. Source: RISI

## Linerboard and Kraft Paper Table I

	2003	2002
Production — tonnes	279,562	410,196
Shipments — tonnes	290,536	395,076
Capital Expenditures — \$millions	8	8
Benchmark Price — linerboard — (per tonne) <sup>1</sup>	US\$ 408	US\$ 464
Benchmark Price — kraft paper — (per tonne) <sup>1</sup>	US\$ 680	US\$ 730

1. Source: West Fraser database

## Newsprint — (West Fraser's share) Table J

	2003	2002
Production — tonnes	127,317	128,394
Shipments — tonnes	126,178	131,930
Capital Expenditures — \$millions	2	2
Benchmark Price — (per tonne) <sup>1</sup>	US\$ 480	US\$ 450

1. West Fraser database



incidents declined. Gains were made in paper machine efficiency and average daily production increased approximately 5% after adjusting for the days lost during the strike. In May, a new general manager was appointed for the mill. His experience and leadership are important as West Fraser is committed to further improving the operations at this mill.

Capital expenditures in the year amounted to \$7.8 million. Although the capital program was disrupted by the strike, several productivity improvement projects were completed.

2003 was the third successive year of weak demand for linerboard and U.S. dollar prices declined a further 10%. While the strike reduced shipments, the well-accepted quality of Eurocan linerboard ensured continued support from customers in all markets. Export kraft paper markets were strong in the first half of the year but weakened substantially in the second half due to a sharp decline in demand.

An improving U.S. economy and a weaker U.S. dollar may result in some revitalization of U.S. production of manufactured goods. As a consequence, demand for packaging for these goods should support modest price improvements for linerboard. Although a US\$40 price increase has been announced for March 1, 2004, it is expected to be implemented during the second quarter. Kraft paper

markets are forecast to remain weak in the first half but an overall improvement in paper and packaging markets should translate into improved pricing in the second half for all products, including kraft paper.

### NEWSPRINT

Newsprint production was slightly lower in 2003 as a result of 12 days of downtime due to a mechanical failure. With this exception, the mill operated well, establishing daily production records. ANC was again ranked as the #1 newsprint supplier by the majority of its customers.

A much tighter supply and demand balance resulting from slightly higher consumption of newsprint and significant capacity closures by major North American newsprint producers led to price increases in both the spring and fall. Several major producers have announced price increases for the first quarter of 2004. Analysts expect that the continuing recovery in the United States will enable the industry to maintain the increases to date and perhaps issue further price increases later in the year.

### SAFETY

Safety performance as measured by the number of incidents was marginally better than in 2002, but was marred by two tragic accidents in the lumber division. West Fraser nevertheless achieved an 8.43 rating under the Medical Incident Rating system that the industry uses to follow the frequency and severity of accidents or injuries, compared to a 9.14 rating in 2002. Although this rating is at the average of the Canadian industry, improvements are required and considerable attention will be directed to safety in the coming year. A board safety committee has been formed to oversee the redoubling of efforts to ensure that West Fraser's safety programs conform to the highest standards, both in their design and in their implementation.

### REVENUE AND EARNINGS COMPARISON

Net sales and EBITDA decreased from the previous year by \$124.1 million and \$193.0 million respectively, mostly due to the significant strengthening of the Canadian dollar. The average \$Cdn/\$US exchange rate moved from 1.57 in 2002 to 1.40 in 2003

### Williams Lake



Graeme McIntosh, silviculture supervisor

Revenue and Earnings Comparison (\$ millions)		Table K	
	2003	2002	
<b>Net Sales</b>	<b>\$ 1,508.1</b>	<b>\$ 1,632.2</b>	
Net Sales by Product			
– Lumber	860.7	930.8	
– Panels	198.8	216.7	
– Pulp & Paper	448.6	484.7	
<b>Total EBITDA</b>	<b>\$ 151.3</b>	<b>\$ 344.3</b>	
EBITDA by Product			
– Lumber	98.9	193.6	
– Panels	36.9	70.4	
– Pulp & Paper	26.9	87.0	

reducing net sales and EBITDA by approximately \$145.0 million. Also, softwood lumber duty charges were higher in 2003 by \$69.6 million and the strike at the Kitimat mill caused a 26% reduction in its shipments. However, these factors were partly offset by increased lumber productivity and shipments, and lower per unit lumber production costs. Other factors affecting results included higher gas costs compared to 2002, lower prices for MDF and higher prices for plywood.

Interest expense decreased by \$15.7 million from the previous year due to debt repayments of US\$150.0 million in 2002 and US\$12.5 million in 2003. The strengthening Canadian dollar resulted in an exchange gain on long-term debt of \$40.8 million compared to \$5.5 million in 2002. Interest

income of \$6.8 million (2002 - \$6.1 million) was earned on short-term investments at prevailing interest rates.

Total tax and tax-like levies and charges were as shown in Table L.

Tax and Tax-like Levies (\$ millions)		Table L	
	2003	2002	
Income Tax	\$ 8.4	\$ 60.8	
Capital Tax	2.1	1.2	
Canada Pension Plan	6.9	6.4	
Employment Insurance	3.9	4.2	
Property Tax	15.2	13.9	
Social Service Tax	9.9	9.6	
Stumpage & Royalties	68.2	86.8	
Workers' Compensation	6.6	4.1	
Other	1.4	1.9	
<b>Total</b>	<b>\$ 122.6</b>	<b>\$ 188.9</b>	

With the exception of income tax, these payments do not vary directly with profitability.

The 2003 provision for income taxes was a recovery of \$6.9 million (2002 - \$56.2 million expense). Note 17 to the accompanying financial statements explains the variance from the statutory tax rate.

Diluted earnings per share from continuing operations were \$1.16 in 2003 (2002 - \$3.47) and diluted earnings per share including discontinued operations were \$1.16 in 2003 (2002 - \$3.70).

Selected Quarterly Information (\$ millions, except earnings per share (EPS) amounts)		Table M							
	2003				2002				
	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31	
<b>Continuing Operations</b>									
Net Sales	\$ 361.4	\$ 382.3	\$ 379.0	\$ 385.4	\$ 404.8	\$ 427.8	\$ 420.2	\$ 379.4	
Earnings	34.3	3.1	(5.2)	10.9	27.1	4.3	71.0	26.6	
Basic EPS <sup>1</sup>	0.93	0.09	(0.14)	0.29	0.74	0.12	1.93	0.72	
Diluted EPS <sup>1</sup>	0.92	0.09	(0.14)	0.29	0.74	0.12	1.91	0.71	
<b>After Discontinued Operations</b>									
Earnings	34.3	3.1	(5.2)	10.9	35.6	4.3	71.0	26.6	
Basic EPS <sup>1</sup>	0.93	0.09	(0.14)	0.29	0.96	0.12	1.93	0.72	
Diluted EPS <sup>1</sup>	0.92	0.09	(0.14)	0.29	0.96	0.12	1.91	0.71	

1. 2002 restated for 10% stock dividend.



### FOURTH QUARTER

Net sales were lower in the fourth quarter compared to the same period last year, primarily because of the strengthening of the Canadian dollar, which reduced sales by approximately \$57.0 million.

Lumber EBITDA increased in the quarter compared to 2002, despite the strength of the Canadian dollar, due to higher shipments and sales prices and lower unit costs of production. EBITDA from the panels operations was somewhat lower than the same period in 2002, with higher plywood prices

largely offset by lower MDF prices.

Pulp and paper EBITDA was poor, due mostly to the continued effects of the Kitimat strike. Although the strike ended in September, shipments of linerboard and kraft paper were 27% lower in the fourth quarter compared to the same period in 2002, reflecting the rebuilding of its customer base and overall poor market conditions. The pulp operations, with higher shipments and prices and newsprint operations with higher prices were solid contributors to EBITDA, despite the strong Canadian dollar.

(\$ millions)		Table N	
	Q4 - 2003	Q4 - 2002	
<b>Net sales</b>	\$ 361.4	\$ 404.8	
<b>EBITDA</b>	\$ 67.7	\$ 70.5	
Operating earnings	\$ 31.8	\$ 34.9	
Interest expense	(3.9)	(4.9)	
Exchange gain on long-term debt	7.2	1.4	
Other income (expense)	5.6	(0.8)	
Provision for income taxes	(6.4)	(3.5)	
Earnings from continuing operations	34.3	27.1	
Earnings from discontinued operations	—	8.5	
<b>Earnings</b>	\$ 34.3	\$ 35.6	

		Table O	
	Q4 - 2003	Q4 - 2002	
<b>Production</b>			
Lumber — Mfbm	641,275	605,130	
MDF — Msf (3/4" basis)	67,612	65,935	
Plywood — Msf (3/8" basis)	61,201	56,840	
BCTMP — tonnes	133,501	117,048	
Linerboard and Kraft Paper — tonnes	114,885	115,940	
Newsprint — tonnes	32,872	32,363	
<b>Shipments</b>			
Lumber — Mfbm	666,012	620,389	
MDF — Msf (3/4" basis)	64,051	56,035	
Plywood — Msf (3/8" basis)	52,217	57,755	
BCTMP — tonnes	127,517	104,340	
Linerboard and Kraft Paper — tonnes	74,250	101,815	
Newsprint — tonnes	32,682	33,389	
<b>Net Sales</b> — \$millions			
Lumber	204.1	223.3	
Panels	49.5	47.7	
Pulp & Paper	107.8	133.8	
<b>EBITDA</b> — \$millions			
Lumber	40.8	21.7	
Panels	11.0	14.7	
Pulp & Paper	15.7	35.9	
<b>\$CDN/\$US — average</b>	<b>1.32</b>	<b>1.57</b>	

## Williams Lake



Larry Frost, *letourneau operator*

## Alberta Plywood



Angel Paul, *line attendant*

### SIGNIFICANT MANAGEMENT JUDGMENTS AFFECTING FINANCIAL RESULTS

The preparation of financial statements requires management to make estimates and assumptions and to select accounting policies that affect the amounts reported in the financial statements. The significant accounting policies followed are disclosed in note 1 to the audited financial statements included in this annual report. The following are the judgments considered most significant:

#### ASSET VALUATION

West Fraser believes that the frequency of technological changes in its manufacturing processes needs to be reflected in its amortization periods. Accordingly, West Fraser amortizes its manufacturing equipment and machinery over 10 to 20 years, with sawmill machinery and equipment averaging 10 to 12 years. Purchased timber rights are amortized over periods not exceeding 60 years. In addition to the appropriateness of the amortization rates, West Fraser periodically reviews estimated future cash flows from long-lived assets as part of its review of asset values.

#### REFORESTATION OBLIGATION

West Fraser's Canadian operations are required by provincial regulations to carry out reforestation to ensure re-establishment of the forest after harvesting. Reforested areas must be tended for a period sufficient to ensure that they are well established.

Although the time to meet legal requirements depends on a variety of factors, in West Fraser's operating areas it usually takes 12 to 15 years. Estimated total cost of reforestation is accrued when logging takes place. These estimates are reviewed annually and adjusted if required. At December 31, 2003 the reforestation obligation accrued in the financial statements was \$93.7 million, comprised of a current portion of \$30.8 million, expected to be spent in 2004, and a long-term portion of \$62.9 million.

#### SHARE-BASED COMPENSATION

West Fraser has granted share options to certain directors, officers and senior employees. Effective July 2003, West Fraser amended its share option plan to allow holders of share options to elect to receive cash in lieu of purchasing shares. The cash payment is to equal the difference between the exercise price of the option and the market price of Common shares on the date of exercise. The amendment was accounted for prospectively and a selling, general and administrative expense of \$8.9 million was recorded for options outstanding. In subsequent periods this will be adjusted to reflect the changes in the share prices and number of options outstanding.

#### PENSION ASSUMPTIONS

West Fraser maintains defined benefit pension plans for many of its employees. Future funding



requirements and the expense for accounting purposes depend on assumptions made by management as well as on actual returns experienced on pension assets. Management makes assumptions it believes to be conservative. The discount rate used in valuing the pension liabilities was decreased from 6.50% to 6.25% which increased the reported pension liability by approximately \$10 million. Table P shows the significant assumptions adopted for the Company.

Pension Assumptions		Table P
	2003	2002
Discount rate	6.25%	6.50%
Expected rate of return	7.00%	7.00%
Compensation increase	4.00%	4.00%

**CHANGE IN ACCOUNTING POLICY**

The Canadian Institute of Chartered Accountants has issued recommendations, effective January 1, 2004, to require that asset retirement obligations be recorded at fair value, with subsequent changes recognized in income. Fair value is based on the present value of the future expected cash flows related to the obligations. The revised policy will impact West Fraser's reforestation obligation which is not presently measured at fair value. Upon initial application of the policy, West Fraser will record a credit to opening retained earnings. This change in accounting policy is not expected to have any impact on future cash requirements or significant impact on reforestation expense.

**CORPORATE GOVERNANCE**

In 2002, the Company adopted a comprehensive corporate governance policy, which may be viewed on its website: [www.westfraser.com](http://www.westfraser.com). In 2003, the Company's Board of Directors established a Governance & Nominating Committee, developed and adopted a formal Charter for its Audit Committee, approved job descriptions for the Board Chair and President & Chief Executive Officer and undertook its first formal review of Board procedures and practices. In addition, non-management directors meet regularly without management representatives present. Non-voting membership of the Audit Committee has been introduced in response to proposed regulations and guidelines concerning the composition of audit committees for Canadian companies.

It is expected that the regulations under Bill 198 proposed by the Ontario Securities Commission will be enacted in early 2004. If passed into law as currently proposed, Bill 198 will require that, beginning with filings related to the first quarter of 2004, the Chief Executive Officer and the Chief Financial Officer certify that they have reviewed the filing, that the filing does not contain any untrue statement of a material fact or omit a material fact and that based on their knowledge, the financial statements together with other financial information included in the filings are, in all material respects, a fair presentation. Management has put in place

**Seehta Sawmill**



(L to R) Clarence Fournier, welder, Benny Beuckert, chip truck driver

**Ranger Board**



Jerry Meyer, E & I technician

## WestPine MDF



Maintenance crew 8-year accident free. Back row (L to R) Dave Berg, Dan Turcotte, Jim Murray, Mario Cuglietta. Front row (L to R) Richard Cole, Tom Harmon, Steve Bradford, Larry Harrison, Geoff Ansell, Chris Berg, Trevor Patchett

systems and reporting structures to meet the certification requirements for 2004.

Financial filings may be reviewed at [www.sedar.com](http://www.sedar.com) and West Fraser Common shares are listed on the Toronto Stock Exchange under the symbol: **WFT**.

### CAPITAL STRUCTURE

The combined number of Common shares and Class B Common shares outstanding increased to 36,856,714 at December 31, 2003 (2002 – 33,483,229). Most of the increase was from the issuance of a 10% stock dividend effective March 14, 2003.

All of West Fraser's debt, other than current borrowings for ANC, is unsecured and ranks equally in right of payment. On December 31, 2003, the ratio of West Fraser's total debt, less cash and short-term investments, to total capitalization was 0.03 (December 31, 2002 – 0.11).

West Fraser's fixed-interest term debt is rated as investment grade by leading rating agencies. The ratings were unchanged from 2002 and the outlook remained stable during 2003. They are currently as shown in Table Q.

Agency	Rating	Table Q
Dominion Bond Rating Service	BBB	
Moody's	BAA2	
Standard & Poor's	BBB	

### ACQUISITIONS

In May 2003, West Fraser acquired timber rights having an AAC of 116,688 m<sup>3</sup> and a non-operating sawmill in Smithers, British Columbia for a net cost of \$6.2 million.

In November 2002, West Fraser purchased the other 50% joint venture interest in QRP for \$0.3 million.

### CAPITAL REQUIREMENTS AND LIQUIDITY

West Fraser's cash requirements, other than for operating purposes, are primarily for interest, repayment of debt, additions to property, plant and equipment, acquisitions and payment of dividends. In years without a major acquisition, cash on hand and cash provided by operations have normally been sufficient to meet these requirements.

In 2003, additions to property, plant and equipment and acquisitions amounted to \$85.4 million (2002 – \$123.4 million). Proceeds from disposal of property, plant and equipment other than from discontinued operations were \$17.5 million (2002 – \$6.3 million) and proceeds from other asset sales were \$30.9 million (2002 – \$nil). There was no cash provided from discontinued operations in 2003 (2002 – \$106.7 million).

A debt repayment of US\$12.5 million was made in 2003 and another of US\$10.0 million will be made in 2004.



**Chasm Sawmill**



(L to R) Heiko Spreng, sawfiler, Mike Balachanoff, sawfitter

On December 31, 2003, West Fraser had unused credit facilities of approximately \$275.0 million in unsecured demand facilities and cash and short-term investments of \$265.9 million (2002 - \$192.9 million). It is expected that cash on hand and funds provided by operations will meet all West Fraser's cash requirements in 2004 for planned additions to property, plant and equipment, debt repayment, interest and dividends.

Table R summarizes West Fraser's financial contractual obligations for each of the next five years and thereafter.

Fraser is not hedging its foreign exchange exposure with financial forward or option contracts.

During 2003, the U.S. dollar traded at between Cdn\$1.58 and Cdn\$1.28, with an average of Cdn\$1.40 (2002-between Cdn\$1.61 and Cdn\$1.51 with an average of Cdn\$1.57).

**U.S. TRADE DISPUTE**

In April and May 2002, U.S. trade agencies (the Department of Commerce ("DOC"), and International Trade Commission ("ITC")) completed an investigation into allegations by the U.S. Industry that Canada was subsidizing softwood lumber products and dumping them into the U.S. market. This resulted in the imposition of cash duty deposits effective May 22, 2002. Preliminary duty liabilities that had accrued from May 19, 2001 to May 21, 2002 were cancelled and all bonds deposited during that period were returned.

The determination in the countervail ("CVD") investigation resulted in a duty deposit rate of 18.79% for shipments from all regions of Canada except the Maritime provinces. The antidumping ("ADD") investigation reviewed shipments from West Fraser and

**Contractual Obligations at December 31, 2003<sup>1</sup> (\$millions)** **Table R**

<b>Total</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>Thereafter</b>	<b>Total</b>
Long-term debt	\$13.0	\$162.1	\$ —	\$124.9	\$ —	\$ —	\$300.0
Operating leases	1.4	0.7	0.4	0.2	0.1	—	2.8
Capital asset commitments	4.0	—	—	—	—	—	4.0
Other	7.2	7.2	7.2	—	—	—	21.6
	\$25.6	\$170.0	\$7.6	\$125.1	\$0.1	\$ —	\$328.4

1. Contractual obligations means an enforceable agreement to purchase goods or services on specified terms but does not include reforestation obligations, energy purchases under various agreements, accounts payable in the ordinary course of business or contingent amounts payable.

**RISKS AND UNCERTAINTIES**

**FOREIGN EXCHANGE**

Most of West Fraser's sales are at prices that, although denominated in a variety of currencies, are generally based on prevailing U.S. dollar prices. This results in significant earnings sensitivity to changes in the U.S. - Canadian dollar exchange rate. Also, payment terms for offshore sales may be up to 180 days and exchange rate fluctuations in the period between purchase and payment may expose West Fraser to greater currency risk. Currently, West

five other major lumber producers, and assigned each a specific ADD rate. All other producers were assigned the weighted average of the six company-specific ADD rates. West Fraser's ADD deposit rate was determined to be 2.18%, while the average rate was 8.47%. Duty deposits must be paid in cash to the U.S. Treasury as shipments cross the border. Final duties are determined through an annual administrative review process that investigates actual shipments for each 12-month period from May 2002.

The federal and provincial governments and

the Canadian industry all categorically deny the U.S. allegations of subsidy and dumping and have initiated appeals under the North American Free Trade Agreement (“NAFTA”) and to the World Trade Organization (“WTO”).

During 2003, Canadian appeals through WTO and NAFTA resulted in several interim decisions that favoured Canada’s position. Most significant was a NAFTA panel decision on September 5, 2003 that for substantive reasons rejected the threat of injury determination by the ITC. If the NAFTA position is upheld through the appeal process, then the DOC must withdraw both the CVD and ADD cases, stop the collection of duty deposits, and refund all deposits paid with interest.

The second significant decision, reached by both NAFTA and WTO, rejected the use of cross-border comparisons by the DOC. These comparisons of U.S. and Canadian timber price differentials are used to calculate the implied subsidies that form the basis of the DOC’s calculation of CVD rates. DOC responded to this rejection on January 12, 2004 and revised its CVD deposit rate to 13.23%. A NAFTA panel will consider this revised DOC determination by the middle of April 2004. Attempts to find a negotiated settlement continued throughout 2003. The objective is to reach an interim agreement that will ultimately lead to unfettered access to the U.S. market. A negotiated solution could involve quotas and result in changes to provincial timber tenure and policy and pricing regimes, especially in British Columbia. It is not possible to predict how such changes might affect West Fraser or the forest industry in Canada. Neither the final outcome nor the time required to resolve the dispute can be determined at this time.

#### **FIRST NATIONS CLAIMS**

Recent decisions of British Columbia courts have identified a duty of the provincial government to consult with potentially affected First Nations’ groups whenever the province deals with public rights. The duty had not previously been recognized by the province, and its nature, extent and implications are uncertain. West Fraser has historically had good relations with First Nations groups in its operating areas, and expects that discharging this duty will result

in increased dealings with First Nations groups in connection with its operations.

During 2003, the British Columbia government initiated a new policy to pursue accommodation agreements with interested First Nations pending conclusion and ratification of comprehensive land claim settlements. These agreements may involve cash payments as well as access to timber where it is appropriate. West Fraser may pursue timber purchase agreements with various First Nations groups where they are of mutual benefit.

Failure of the government to adequately discharge its obligations to First Nations groups may affect the validity of its actions in dealing with public rights. The resulting uncertainty presents a risk to those relying upon the validity of a grant of public rights, such as timber harvesting rights. This uncertainty may be alleviated by government action, the negotiation of treaties with First Nations groups and further judgments of the courts.

Management does not expect that there will be any land claim settlements in 2004 that will affect West Fraser’s Alberta operating areas.

#### **PINE BEETLE INFESTATION**

Over the last several years, a mountain pine beetle infestation has grown rapidly in the central interior of British Columbia. Unless the spread collapses, timber supply in the next 15 years could be reduced by up to 30% of pre-epidemic levels. For more information on this topic see “Management’s Discussion & Analysis – Lumber”.

#### **ENVIRONMENT**

The section of this Annual Report entitled “West Fraser Environmental Report” is incorporated herein by reference.

#### **EARNINGS SENSITIVITY**

West Fraser’s earnings are sensitive to changes in world economic conditions, primarily those in North America, Europe and the Far East. Most of its revenues are from sales of commodities for which prices are sensitive to variations in supply and demand. Since most of these sales are in foreign currencies, mainly U.S. dollars, currency exchange fluctuations are a major factor.



**Earnings Sensitivity to Key Variables – based on year-end capacities (\$ millions) Table S**

Factor	Variation	Change in Earnings
Lumber price <sup>1</sup>	US\$50 change per Mfbm	\$ 79
Plywood price	US\$50 change per Msf	\$ 11
MDF price	US\$50 change per Msf	\$ 12
BCTMP price	US\$50 change per tonne	\$ 21
Linerboard price	US\$50 change per tonne	\$ 14
Kraft paper price	US\$50 change per tonne	\$ 5
Newsprint price	US\$50 change per tonne	\$ 6
U.S.-Canadian \$ exchange rate <sup>2</sup>	US\$0.01 change per Cdn\$	\$ 11
Log cost	C\$10 change per m <sup>3</sup>	\$ 64

1. Excludes impact of softwood lumber duties

2. Excludes exchange impact on translation of long-term debt and U.S. operations

West Fraser's principal raw material is timber. In Alberta, stumpage charges on logs harvested from its timber tenures are indexed to the market price of lumber. In British Columbia, under the new Forestry Revitalization Plan, it is proposed that stumpage will be based on auction-based timber pricing by the end of 2004. Prices paid for logs obtained on the open market are the result of competitive bidding between mills. In West Fraser's operations in the United States, approximately 65% of the required log volume is obtained at market prices under a long-term contract and the balance through market purchases.

Interest rates, particularly in the United States, have a significant effect on house construction or renovation activity, which in turn influences the demand for and price of building materials.

**BUSINESS OUTLOOK – 2004**

West Fraser's financial performance is largely dependent on commodity prices and the value of the

Canadian dollar in relation to the U.S. dollar. Several other factors could also significantly affect its financial results in 2004. These include the outcome of the Canada-U.S. softwood lumber trade dispute, continued changes in government policies affecting timber harvesting and pricing, the cost structure of West Fraser's various manufacturing units, and acquisitions it might undertake.

The U.S. economy performed well in 2003 and is expected to continue to benefit from the stimulative fiscal measures. Continuing low inflation will minimize any interest rate increases and, historically, rate hikes are unusual during a presidential election year. Over the last 6 years, housing starts have been extremely strong and the low interest environment is expected to extend this run. Good lumber and structural panel demand should therefore continue throughout the year.

MDF markets in North America began to show improvement by the end of 2003 and are expected to continue to grow. Also, the extensive customer development work done in the past few years by West Fraser will result in improved sales through a higher-value grade mix.

For most pulp and paper products, price improvements are expected this year, driven largely by a stronger U.S. economy.

West Fraser will be embarking on a major capital expenditure program in the year, with the greatest emphasis on the sawmills. This is expected to increase lumber production by about 10%.

West Fraser's very strong financial position provides the basis to consider growth opportunities as they may arise.

**Fraser Lake Sawmill**



Phil Canaday, sawmill superintendent

**Joyce Sawmill**



John Pimpton, fork lift operator