

MERCER INTERNATIONAL INC.  
Form 10-Q  
October 26, 2017

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the quarterly period ended September 30, 2017**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File No.: 000-51826**

**MERCER INTERNATIONAL INC.**

*(Exact name of Registrant as specified in its charter)*

**Washington**  
*(State or other jurisdiction*

**47-0956945**  
*(I.R.S. Employer*

*of incorporation or organization)*

*Identification No.)*

**Suite 1120, 700 West Pender Street, Vancouver, British Columbia, Canada, V6C 1G8**

*(Address of office)*

**(604) 684-1099**

*(Registrant's telephone number, including area code)*

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the *Securities Exchange Act of 1934* during the preceding 12 months (or for such shorter period that the Registrant

was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  
NO

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months or for such shorter period that the registrant was required to submit and post such files). YES  
NO

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definitions of large accelerated filer , accelerated filer , non-accelerated filer , smaller reporting company and emerging growth company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer      Accelerated Filer      Non-Accelerated Filer      Smaller Reporting Company

Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
YES      NO

The Registrant had 65,017,288 shares of common stock outstanding as at October 25, 2017.

**PART I. FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

**MERCER INTERNATIONAL INC.**

**INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2017**

**(Unaudited)**

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QUARTERLY REPORT - PAGE 2

**MERCER INTERNATIONAL INC.****INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)****(In thousands of U.S. dollars, except per share data)**

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Revenues	\$ 305,498	\$ 237,941	\$ 831,459	\$ 709,929
Costs and expenses				
Operating costs, excluding depreciation and amortization	229,314	180,124	633,180	550,293
Operating depreciation and amortization	22,568	17,923	62,205	52,810
Selling, general and administrative expenses	12,327	10,073	35,312	32,128
Operating income	41,289	29,821	100,762	74,698
Other income (expenses)				
Interest expense	(13,513)	(12,791)	(40,712)	(38,718)
Loss on settlement of debt (Note 5(a))			(10,696)	(454)
Other income (expenses)	(1)	5	1,308	109
Total other expenses	(13,514)	(12,786)	(50,100)	(39,063)
Income before provision for income taxes	27,775	17,035	50,662	35,635
Provision for income taxes	(6,632)	(5,109)	(21,897)	(19,181)
Net income	\$ 21,143	\$ 11,926	\$ 28,765	\$ 16,454
Net income per common share				
Basic	\$ 0.33	\$ 0.18	\$ 0.44	\$ 0.25
Diluted	\$ 0.32	\$ 0.18	\$ 0.44	\$ 0.25
Dividends declared per common share	\$ 0.115	\$ 0.115	\$ 0.345	\$ 0.345

**INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited)****(In thousands of U.S. dollars)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Net income	\$ 21,143	\$ 11,926	\$ 28,765	\$ 16,454
Other comprehensive income (loss), net of taxes <sup>(1)</sup>				
Foreign currency translation adjustment	37,957	13,355	107,597	38,710
Change in unrecognized losses and prior service costs related to defined benefit pension plan	302	291	904	870
Change in unrealized gains/losses on marketable securities	53	(6)	58	(4)
Other comprehensive income (loss), net of taxes <sup>(1)</sup>	38,312	13,640	108,559	39,576
Total comprehensive income	\$ 59,455	\$ 25,566	\$ 137,324	\$ 56,030

(1) Balances are net of tax effects of \$nil in all periods.

*The accompanying notes are an integral part of these Interim Consolidated Financial Statements.*

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**MERCER INTERNATIONAL INC.****INTERIM CONSOLIDATED BALANCE SHEETS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)**

	<b>September 30, 2017</b>	<b>December 31, 2016</b>
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 157,217	\$ 136,569
Restricted cash (Note 11)	2,125	4,327
Accounts receivable	181,062	123,892
Inventories	164,374	133,451
Prepaid expenses and other	8,827	3,612
Total current assets	513,605	401,851
Property, plant and equipment, net	844,502	738,276
Intangible and other assets	26,605	7,591
Deferred income tax	1,170	10,990
Total assets	\$ 1,385,882	\$ 1,158,708
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities		
Accounts payable and other	\$ 142,201	\$ 92,133
Pension and other post-retirement benefit obligations	1,115	1,037
Total current liabilities	143,316	93,170
Debt	669,012	617,545
Pension and other post-retirement benefit obligations	26,283	25,084
Capital leases and other	27,696	26,467
Deferred income tax	21,574	17,314
Total liabilities	887,881	779,580
Shareholders equity		
Common shares \$1 par value; 200,000,000 authorized;		
65,017,000 issued and outstanding (2016 64,694,000)	64,974	64,656
Additional paid-in capital	337,330	333,673
Retained earnings	172,407	166,068

Accumulated other comprehensive loss	(76,710)	(185,269)
Total shareholders' equity	498,001	379,128
Total liabilities and shareholders' equity	\$ 1,385,882	\$ 1,158,708

Commitments and contingencies (Note 13)

Subsequent event (Note 9)

*The accompanying notes are an integral part of these Interim Consolidated Financial Statements.*

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## MERCER INTERNATIONAL INC.

## INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands of U.S. dollars)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Cash flows from (used in) operating activities				
Net income	\$ 21,143	\$ 11,926	\$ 28,765	\$ 16,454
Adjustments to reconcile net income to cash flows from operating activities				
Depreciation and amortization	22,673	18,031	62,519	53,212
Deferred income tax provision	4,184	3,343	12,589	12,290
Loss on settlement of debt			10,696	454
Defined benefit pension plan and other post-retirement benefit plan expense	549	446	1,615	1,320
Stock compensation expense	774	972	1,525	2,627
Other	783	1,577	1,308	2,099
Defined benefit pension plan and other post-retirement benefit plan contributions	(458)	(421)	(1,309)	(1,305)
Changes in working capital				
Accounts receivable	1,584	(3,533)	(42,130)	8,968
Inventories	(14,043)	(7,695)	(9,912)	3,293
Accounts payable and accrued expenses	(1,906)	11,980	41,929	11,877
Other	(1,496)	(190)	(4,338)	(110)
Net cash from (used in) operating activities	33,787	36,436	103,257	111,179
Cash flows from (used in) investing activities				
Purchase of property, plant and equipment	(14,342)	(8,562)	(42,249)	(28,977)
Purchase of intangible assets	(394)	(208)	(799)	(1,144)
Acquisition of Friesau Facility (Note 2)			(61,627)	
Other	(381)	(678)	(304)	69
Net cash from (used in) investing activities	(15,117)	(9,448)	(104,979)	(30,052)
Cash flows from (used in) financing activities				
Repurchase of notes			(234,945)	(23,079)
Proceeds from issuance of notes			250,000	
Proceeds from revolving credit facility		7,662	26,525	7,662
Dividend payments	(7,477)	(7,440)	(22,389)	(22,293)
Payment of debt issuance costs			(6,132)	
Payment of interest rate derivative liability			(3,789)	(5,852)



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Other	(389)	420	569	(583)
Net cash from (used in) financing activities	(7,866)	642	9,839	(44,145)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	3,895	1,265	10,329	3,539
Net increase in cash, cash equivalents and restricted cash	14,699	28,895	18,446	40,521
Cash, cash equivalents and restricted cash, beginning of period	144,643	120,485	140,896	108,859
Cash, cash equivalents and restricted cash, end of period	\$ 159,342	\$ 149,380	\$ 159,342	\$ 149,380
Supplemental cash flow disclosure				
Cash paid for interest	\$ 8,430	\$ 1,396	\$ 29,311	\$ 26,031
Cash paid for income taxes	\$ 2,797	\$ 2,954	\$ 8,001	\$ 12,265

*The accompanying notes are an integral part of these Interim Consolidated Financial Statements.*

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**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 1. The Company and Summary of Significant Accounting Policies**

**Nature of Operations and Basis of Presentation**

The Interim Consolidated Financial Statements contained herein include the accounts of Mercer International Inc. ( Mercer Inc. ) and all of its subsidiaries (collectively the Company ). The Company s shares of common stock are quoted and listed for trading on both the NASDAQ Global Market and the Toronto Stock Exchange.

The Interim Consolidated Financial Statements have been prepared by the Company pursuant to the rules and regulations of the United States Securities and Exchange Commission (the SEC ). The year-end Consolidated Balance Sheet data was derived from audited financial statements. The footnote disclosure included herein has been prepared in accordance with accounting principles generally accepted for interim financial statements in the United States ( GAAP ). The unaudited Interim Consolidated Financial Statements should be read together with the audited Consolidated Financial Statements and accompanying notes included in the Company s latest Annual Report on Form 10-K for the fiscal year ended December 31, 2016. In the opinion of the Company, the unaudited Interim Consolidated Financial Statements contained herein contain all adjustments necessary for a fair statement of the results of the interim periods included. The results for the periods included herein may not be indicative of the results for the entire year.

In these Interim Consolidated Financial Statements, unless otherwise indicated, all amounts are expressed in United States dollars ( U.S. dollars or \$ ). The symbol € refers to euros and the symbol C\$ refers to Canadian dollars.

**Use of Estimates**

Preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant management judgment is required in determining the accounting for, among other things, pension and other post-retirement benefit obligations, deferred income taxes (valuation allowance and permanent reinvestment), depreciation and amortization, future cash flows associated with impairment testing for long-lived assets, the allocation of the purchase price in a business combination to the assets acquired and liabilities assumed, legal liabilities and contingencies. Actual results could differ materially from these estimates, and changes in these estimates are recorded when known.

**New Accounting Pronouncements**

*Accounting Pronouncements Implemented*

In July 2015, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update 2015-11, Simplifying the Measurement of Inventory ( ASU 2015-11 ) which requires that inventory within the scope of this update, including inventory stated at average cost, be measured at the lower of cost and net realizable value. This update is effective for financial statements issued for fiscal years beginning after December 15, 2016, with early adoption permitted as of the beginning of an interim or annual reporting period. The adoption of ASU 2015-11 did not

impact the Company's financial position.

In March 2016, the FASB issued Accounting Standards Update 2016-09, Improvements to Employee Share-Based Payment Accounting ( ASU 2016-09 ) which simplifies several aspects of accounting for share-based payment transactions including income tax consequences, classification of awards as either equity or liabilities, classification on the statement of cash flows and accounting for forfeitures. This update is effective for financial statements issued for fiscal years beginning after December 15, 2016. The adoption of ASU 2016-09 did not impact the Company's financial position.

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**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

*Accounting Pronouncements Not Yet Implemented*

In May 2014, the FASB issued Accounting Standards Update 2014-09, Revenue Recognition Revenue from Contracts with Customers ( ASU 2014-09 ) that requires companies to recognize revenue when a customer obtains control rather than when companies have transferred substantially all risks and rewards of a good or service. In 2016 the FASB issued the following Accounting Standards which further affect the guidance of ASU 2014-09:

March 2016: ASU 2016-08, Principal versus Agent Considerations (Reporting Revenue Gross versus Net);

April 2016: ASU 2016-10, Identifying Performance Obligations and Licensing;

May 2016: ASU 2016-12, Revenue from Contracts with Customers: Narrow Scope Improvements and Practical Expedients; and

December 2016: ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers.

These standards are effective for annual reporting periods beginning on or after December 15, 2017 with early adoption permitted at the beginning of an interim or annual reporting period beginning after December 15, 2016. Currently, the Company believes this new standard will not have a material impact on its consolidated financial statements, however, its assessment of this standard is ongoing. The Company expects to adopt this standard as of January 1, 2018.

In February 2016, the FASB issued Accounting Standards Update 2016-02, Leases ( ASU 2016-02 ) which requires lessees to recognize virtually all of their leases on the balance sheet, by recording a right-of-use asset and liability. This update is effective for financial statements issued for fiscal years beginning after December 15, 2018, with early adoption permitted at the beginning of an interim or annual reporting period. The Company is currently assessing the impact the adoption of ASU 2016-02 will have on its consolidated financial statements.

In October 2016, the FASB issued Accounting Standards Update 2016-16, Intra-Entity Transfers of Assets Other Than Inventory ( ASU 2016-16 ) which eliminates the deferral of the tax effects of intra-entity asset transfers other than inventory until the transferred assets are sold to a third party or recovered through use. This update is effective on a modified retrospective approach for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company is currently assessing the impact the adoption of ASU 2016-16 will have on its consolidated financial statements.

In January 2017, the FASB issued Accounting Standards Update 2017-01, Clarifying the Definition of a Business ( ASU 2017-01 ) which revises the definition of a business. When substantially all of the fair value of gross assets acquired is concentrated in a single asset (or a group of similar assets), the asset acquired would not represent a business. This update is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company is currently assessing the impact the adoption of ASU 2017-01 will have on its consolidated financial statements.

In March 2017, the FASB issued Accounting Standards Update 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post-Retirement Benefit Cost ( ASU 2017-07 ) which requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations. This standard is effective for fiscal years beginning after December 15, 2017 and should be applied retrospectively to all periods presented. The Company believes this new standard will not have a material impact on its consolidated financial statements.

In August 2017, the FASB issued Accounting Standards Update 2017-12, Derivatives and Hedging ( ASU 2017-12 ) which expands and refines hedge accounting for both nonfinancial and financial risk components and aligns the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. This standard is effective for fiscal years beginning after December 15, 2018. Early application is permitted in any interim period and all transition requirements and elections should be applied to hedging relationships existing on the date of adoption. The Company believes this new standard will not have a material impact on its consolidated financial statements.

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**MERCER INTERNATIONAL INC.****NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Note 2. Acquisition**

On April 12, 2017, the Company, through its wholly owned subsidiary Mercer Timber Products GmbH ( MTP ) acquired substantially all of the assets of a German sawmill, and a bio-mass power plant, near Friesau, Germany (the Friesau Facility ) for \$61,627 cash. The acquisition of the Friesau Facility presents the Company with the opportunity to expand into the German lumber market and grow its bio-mass energy profile.

The following summarizes the Company's preliminary allocation of the purchase price to the fair value of the assets acquired and liabilities assumed at the acquisition date:

	<b>Purchase Price Allocation</b>
Inventories	\$ 6,917
Property, plant and equipment	37,392
Amortizable intangible assets (a)	17,780
<b>Total assets acquired</b>	<b>62,089</b>
Liabilities assumed - accounts payable and other	462
<b>Net assets acquired</b>	<b>\$ 61,627</b>

(a) Amortizable intangible assets relate to an energy sales agreement, which has a fair value of \$15,970 and an amortization period of 11 years and enterprise resource planning software, which has a fair value of \$1,810 and an amortization period of five years.

The purchase price allocation was based upon a preliminary valuation for all items and may be revised as a result of additional information obtained regarding assets acquired and liabilities assumed, and revisions of provisional estimates of fair value, including, but not limited to, the completion of valuations related to property, plant and equipment and intangible assets. The purchase price allocation will be finalized during the 12 month measurement period following the acquisition date.

The Friesau Facility is a business under GAAP, accordingly the Company began consolidating the results of operations, financial position and cash flows of the Friesau Facility in the Interim Consolidated Financial Statements as of the acquisition date. The amount of the Friesau Facility's revenues included in the Interim Consolidated Statements of Operations for the three and nine month periods ended September 30, 2017 was \$33,140 and \$50,431, respectively. The amount of the Friesau Facility's net income included in the Interim Consolidated Statements of Operations for the three and nine month periods ended September 30, 2017 was \$930 and \$157, respectively. In the nine month period ended September 30, 2017, \$868 of acquisition related costs were recognized in selling, general and administrative expenses in the Interim Consolidated Statements of Operations.

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The following unaudited pro forma information for the three and nine month periods ended September 30, 2017 and 2016, represents the Company's results of operations as if the acquisition of the Friesau Facility had occurred on January 1, 2016. This pro forma information does not purport to be indicative of the results that would have occurred for the periods presented or that may be expected in the future.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenues	\$ 305,498	\$ 276,647	\$ 872,367	\$ 826,048
Net income	\$ 21,143	\$ 13,566	\$ 31,466	\$ 20,506

The unaudited pro forma information for the three and nine month periods ended September 30, 2017 and 2016 includes additional interest expense related to debt issued to finance the acquisition and adjustments related to acquisition costs. The adjustments were immaterial and the nonrecurring items are included in the earliest period presented.

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**MERCER INTERNATIONAL INC.****NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Note 3. Inventories**

	<b>September 30, 2017</b>	<b>December 31, 2016</b>
Raw materials	\$ 50,337	\$ 50,056
Finished goods	49,775	33,510
Spare parts and other	64,262	49,885
	\$ 164,374	\$ 133,451

**Note 4. Accounts Payable and Other**

	<b>September 30, 2017</b>	<b>December 31, 2016</b>
Trade payables	\$ 37,357	\$ 28,815
Accrued expenses	72,947	39,903
Interest payable	13,568	3,916
Interest rate derivative liability	3,109	6,522
Dividends payable	7,477	7,440
Other	7,743	5,537
	\$ 142,201	\$ 92,133

**Note 5. Debt**

	<b>September 30, 2017</b>	<b>December 31, 2016</b>
2022 Senior Notes, unsecured, \$400,000 face value (a)	\$ 394,288	\$ 393,460
2024 Senior Notes, unsecured, \$250,000 face value (a)	245,209	
2019 Senior Notes (a)		224,085
Revolving credit facilities		
75.0 million (b)		
C\$40.0 million (c)		
70.0 million (d)	29,515	
5.0 million (e)		



\$	669,012	\$	617,545
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As at September 30, 2017, the maturities of the principal portion of debt are as follows:

2017	\$
2018	
2019	
2020	
2021	
Thereafter	679,515
	\$ 679,515

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**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

Certain of the Company's debt instruments were issued under agreements which, among other things, may limit its ability and the ability of its subsidiaries to make certain payments, including dividends. These limitations are subject to specific exceptions. As at September 30, 2017, the Company was in compliance with the terms of its debt agreements.

(a) On February 3, 2017, the Company issued \$225,000 in aggregate principal amount of 6.50% senior notes which mature on February 1, 2024 ( 2024 Senior Notes ). The 2024 Senior Notes were issued at a price of 100% of their principal amount. The net proceeds of the offering were \$220,240, after deducting the underwriter's discount and offering expenses. The net proceeds, together with cash on hand, were used to purchase \$227,000 of remaining aggregate principal amount of outstanding 2019 Senior Notes (herein defined below). In connection with this purchase the Company recorded a loss on settlement of debt of \$10,696 in the Interim Consolidated Statement of Operations.

On March 16, 2017, the Company issued an additional \$25,000 in aggregate principal amount of its 2024 Senior Notes. The additional notes were priced at 100% plus accrued interest from February 3, 2017. The net proceeds from the offering were \$24,471, net of the underwriter's discounts, offering expenses and accrued interest. The net proceeds, together with cash on hand, were used to finance the Company's acquisition of the Friesau Facility and for general working capital purposes.

On November 26, 2014, the Company issued \$650,000 of senior notes consisting of \$250,000 in aggregate principal amount of 7.00% senior notes which were to mature on December 1, 2019 ( 2019 Senior Notes ) and \$400,000 in aggregate principal amount of 7.75% senior notes which mature on December 1, 2022 ( 2022 Senior Notes ). The 2019 Senior Notes and 2022 Senior Notes were issued at a price of 100% of their principal amount. Upon their issuance the 2019 Senior Notes and 2022 Senior Notes were recorded at \$635,949 which included debt issuance costs of \$14,051. These costs were proportionally allocated to the 2019 Senior Notes and the 2022 Senior Notes.

In March 2016, the Company purchased \$23,000 in aggregate principal amount of its 2019 Senior Notes. In connection with this purchase the Company recorded a loss on settlement of debt of \$454 in the Interim Consolidated Statement of Operations.

The 2022 Senior Notes and 2024 Senior Notes are general unsecured senior obligations of the Company. They rank equal in right of payment with all existing and future unsecured senior indebtedness of the Company and are senior in right of payment to any current or future subordinated indebtedness of the Company. They are effectively junior in right of payment to all existing and future secured indebtedness, to the extent of the assets securing such indebtedness, and all indebtedness and liabilities of the Company's subsidiaries.

The Company may redeem all or a part of the 2022 Senior Notes and 2024 Senior Notes, upon not less than 30 days or more than 60 days notice, at the redemption prices (expressed as percentages of principal amount) discussed below, plus accrued and unpaid interest to (but not including) the applicable redemption date. The 2022 Senior Notes redemption prices are equal to 105.813% for the twelve month period beginning on December 1, 2017, 103.875% for the twelve month period beginning on December 1, 2018, 101.938% for the twelve month period beginning on

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December 1, 2019, and 100.000% beginning on December 1, 2020 and at any time thereafter. The 2024 Senior Notes redemption prices are equal to 103.250% for the twelve month period beginning on February 1, 2020, 101.625% for the twelve month period beginning on February 1, 2021, and 100.000% beginning on February 1, 2022 and at any time thereafter.

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**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

- (b) A 75.0 million revolving credit facility at the Stendal mill that matures in October 2019. Borrowings under the facility are collateralized by the mill's inventory and accounts receivable and bear interest at Euribor plus 3.50%. As at September 30, 2017, 75.0 million (\$88,545) was available.
- (c) A C\$40.0 million revolving credit facility at the Celgar mill that matures in May 2019. Borrowings under the facility are collateralized by the mill's inventory and accounts receivable and are restricted by a borrowing base calculated on the mill's inventory and accounts receivable. Canadian dollar denominated amounts bear interest at bankers acceptance plus 1.50% or Canadian prime. U.S. dollar denominated amounts bear interest at LIBOR plus 1.50% or U.S. base. As at September 30, 2017, approximately C\$1.7 million (\$1,361) was supporting letters of credit and approximately C\$38.3 million (\$30,690) was available.
- (d) In April 2017, in connection with the acquisition of the Friesau Facility, the Company replaced the 25.0 million revolving credit facility with a new 70.0 million joint revolving credit facility that matures in April 2022. The Rosenthal mill has full access to the available amount under the facility and MTP has access to a maximum of 45.0 million. Borrowings under the facility are collateralized by the borrowers' inventory and accounts receivable and bear interest at Euribor plus 2.95%. As at September 30, 2017, approximately 25.0 million (\$29,515) of this facility was drawn and accruing interest at a rate of 2.95% and approximately 8.4 million (\$9,883) of this facility was supporting bank guarantees leaving approximately 36.6 million (\$43,244) available.
- (e) A 5.0 million revolving credit facility at the Rosenthal mill that matures in December 2018. Borrowings under this facility bear interest at the rate of the three-month Euribor plus 2.50% and are secured by certain land at the Rosenthal mill. As at September 30, 2017 approximately 3.3 million (\$3,910) of this facility was supporting bank guarantees leaving approximately 1.7 million (\$1,993) available.

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## MERCER INTERNATIONAL INC.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(In thousands of U.S. dollars, except share and per share data)

**Note 6. Pension and Other Post-Retirement Benefit Obligations****Defined Benefit Plans**

Included in pension and other post-retirement benefit obligations are amounts related to the Company's Celgar and Rosenthal mills. The largest component of these obligations is with respect to the Celgar mill which maintains a defined benefit pension plan and other post-retirement benefit plans for certain employees (the Celgar Defined Benefit Plans).

Pension benefits are based on employees' earnings and years of service. The Celgar Defined Benefit Plans are funded by contributions from the Company based on actuarial estimates and statutory requirements.

The components of the net benefit costs relating to the Celgar Defined Benefit Plans for the three and nine month periods ended September 30, 2017 and 2016 were as follows:

	Three Months Ended September 30, 2017		2016	
	Pension	Other Post-Retirement Benefits	Pension	Other Post-Retirement Benefits
Service cost	\$ 25	\$ 151	\$ 23	\$ 122
Interest cost	346	245	259	240
Expected return on plan assets	(520)		(489)	
Amortization of unrecognized items	265	37	335	(44)
Net benefit costs	\$ 116	\$ 433	\$ 128	\$ 318

	Nine Months Ended September 30, 2017		2016	
	Pension	Other Post-Retirement Benefits	Pension	Other Post-Retirement Benefits
Service cost	\$ 71	\$ 435	\$ 68	\$ 363
Interest cost	998	706	756	711
Expected return on plan assets	(1,499)		(1,448)	
Amortization of unrecognized items	792	112	1,002	(132)
Net benefit costs	\$ 362	\$ 1,253	\$ 378	\$ 942

**Defined Contribution Plan**

Effective December 31, 2008, the Celgar Defined Benefit Plans were closed to new members. In addition, the defined benefit service accrual ceased on December 31, 2008, and members began to receive pension benefits, at a fixed contractual rate, under a new defined contribution plan effective January 1, 2009. During the three and nine month periods ended September 30, 2017, the Company made contributions of \$213 and \$672, respectively (2016 \$200 and \$509), to this plan.

**Multiemployer Plan**

The Company participates in a multiemployer plan for the hourly-paid employees at the Celgar mill. The contributions to the plan are determined based on a percentage of pensionable earnings pursuant to a collective bargaining agreement. The Company has no current or future contribution obligations in excess of the contractual contributions. During the three and nine month periods ended September 30, 2017, the Company made contributions of \$493 and \$1,539, respectively (2016 \$384 and \$1,167), to this plan.

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## MERCER INTERNATIONAL INC.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(In thousands of U.S. dollars, except share and per share data)

## Note 7. Income Taxes

The income tax provision attributable to income before provision for income taxes in the Interim Consolidated Statements of Operations differs from the amounts computed by applying the U.S. Federal statutory income tax rate of 35% for the three and nine month periods ended September 30, 2017 and 2016 as a result of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
U.S. Federal statutory rate	35%	35%	35%	35%
U.S. Federal statutory rate on income before income taxes	\$ (9,722)	\$ (5,962)	\$ (17,732)	\$ (12,472)
Tax differential on foreign income	2,701	1,719	5,668	3,353
Effect of foreign earnings		1,750		(1,750)
Change in undistributed earnings	(450)		(5,915)	
Valuation allowance	(1,823)	(3,805)	(11,177)	(15,223)
Tax benefit of partnership structure	1,246	1,304	3,692	3,867
Non-taxable foreign subsidiaries	608	575	1,717	1,693
True-up of prior year taxes	(169)	(78)	(279)	(138)
Foreign exchange on valuation allowance	1,241	(329)	2,404	1,347
Foreign exchange on settlement of debt			550	870
Other	(264)	(283)	(825)	(728)
	\$ (6,632)	\$ (5,109)	\$ (21,897)	\$ (19,181)
Comprised of:				
Current income tax provision	\$ (2,448)	\$ (1,766)	\$ (9,308)	\$ (6,891)
Deferred income tax provision	(4,184)	(3,343)	(12,589)	(12,290)
	\$ (6,632)	\$ (5,109)	\$ (21,897)	\$ (19,181)





**MERCER INTERNATIONAL INC.****NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Note 8. Net Income Per Common Share**

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Net income				
Basic and diluted	\$ 21,143	\$ 11,926	\$ 28,765	\$ 16,454
Net income per common share				
Basic	\$ 0.33	\$ 0.18	\$ 0.44	\$ 0.25
Diluted	\$ 0.32	\$ 0.18	\$ 0.44	\$ 0.25
Weighted average number of common shares outstanding:				
Basic <sup>(1)</sup>	64,973,653	64,656,138	64,896,511	64,623,215
Effect of dilutive shares:				
Performance Share Units ( PSUs )	412,995	495,663	429,801	397,447
Restricted shares	7,268	3,353	17,447	20,359
Diluted	65,393,916	65,155,154	65,343,759	65,041,021

(1) For the three and nine month periods ended September 30, 2017, the basic weighted average number of common shares outstanding excludes 43,635 restricted shares which have been issued, but have not vested as at September 30, 2017 (2016 38,000 restricted shares).

The calculation of diluted net income per common share does not assume the exercise of any instruments that would have an anti-dilutive effect on net income per common share. There were no anti-dilutive instruments for the three and nine month periods ended September 30, 2017 and 2016.

**Note 9. Shareholders Equity****Dividends**

During the nine month period ended September 30, 2017, the Company's Board of Directors declared the following quarterly dividends:

<b>Date Declared</b>	<b>Dividend Per Common Share</b>	<b>Amount</b>
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February 9, 2017	\$	0.115	\$	7,472
April 27, 2017		0.115		7,477
July 27, 2017		0.115		7,477
	\$	0.345	\$	22,426

Dividends are paid in the quarter subsequent to the quarter in which they were declared.

In October 2017, the Company's Board of Directors declared a quarterly dividend of \$0.125 per common share. Payment of the dividend will be made on January 4, 2018 to all shareholders of record on December 27, 2017. Future dividends are subject to approval by the Board of Directors and may be adjusted as business and industry conditions warrant.

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**MERCER INTERNATIONAL INC.****NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Stock Based Compensation**

In June 2010, the Company adopted a stock incentive plan which provides for options, restricted stock rights, restricted shares, performance shares, PSUs and stock appreciation rights to be awarded to employees, consultants and non-employee directors. During the nine month period ended September 30, 2017, there were no issued or outstanding options, restricted stock rights, performance shares or stock appreciation rights. In May 2017, the shareholders of the Company approved an additional 2.3 million common shares be available for grant pursuant to the 2010 Plan. As at September 30, 2017, after factoring in all allocated shares, there remain approximately 3.2 million common shares available for grant.

*PSUs*

PSUs comprise rights to receive common shares at a future date that are contingent on the Company and the grantee achieving certain performance objectives. The performance objective period is generally three years. For the three and nine month periods ended September 30, 2017, the Company recognized an expense of \$646 and \$1,201, respectively related to PSUs (2016 - \$882 and \$2,268).

The following table summarizes PSU activity during the period:

	<b>Number of PSUs</b>
Outstanding as at January 1, 2017	2,068,174
Granted	542,788
Vested and issued	(279,515)
Forfeited	(464,289)
Outstanding as at September 30, 2017	1,867,158

*Restricted Shares*

Restricted shares generally vest at the end of one year. For the three and nine month periods ended September 30, 2017, the Company recognized an expense of \$128 and \$324, respectively related to restricted shares (2016 - \$90 and \$359). As at September 30, 2017, the unrecognized compensation cost related to restricted shares was approximately \$343 which will be amortized over the remaining vesting periods.

The following table summarizes restricted share activity during the period:

**Number of Restricted  
Shares**

Outstanding at January 1, 2017	38,000
Granted	43,635
Vested	(38,000)
Outstanding at September 30, 2017	43,635

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**MERCER INTERNATIONAL INC.**
**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Settlement of Short Swing Profit Claim**

In March 2017, the Company and a shareholder entered into a settlement agreement pursuant to which the shareholder paid \$3,000 (net \$2,450 after costs) to the Company to settle a claim by the Company for short swing profits under Section 16(b) in the Exchange Act. The net settlement was classified as additional paid-in-capital.

**Retained Earnings**

The following table summarizes the changes to retained earnings during the period:

	<b>Nine Months Ended September 30, 2017</b>	
Retained earnings at January 1, 2017	\$	166,068
Net income		28,765
Cash dividends declared		(22,426)
Retained earnings at September 30, 2017	\$	172,407

**Accumulated Other Comprehensive Loss**

The components of accumulated other comprehensive loss are as follows:

	<b>Foreign Currency Translation Adjustment</b>	<b>Defined Benefit Pension and Other Post- Retirement Benefit Items</b>	<b>Unrealized Gains / Losses on Marketable Securities</b>	<b>Total</b>
Balance as at January 1, 2017	\$ (170,592)	\$ (14,663)	\$ (14)	\$ (185,269)
Other comprehensive income before reclassifications	107,597		58	107,655
Amounts reclassified from accumulated other comprehensive loss		904		904
Other comprehensive income	107,597	904	58	108,559
Balance as at September 30, 2017	\$ (62,995)	\$ (13,759)	\$ 44	\$ (76,710)

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## MERCER INTERNATIONAL INC.

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(In thousands of U.S. dollars, except share and per share data)

**Note 10. Segment Disclosures**

The Company is managed based on the primary products it manufactures: pulp and wood products. Accordingly, the Company's three pulp mills are aggregated into the pulp business segment, and the Friesau Facility is a separate reportable business segment, wood products.

None of the income or loss items following operating income in the Company's Interim Consolidated Statement of Operations are allocated to the segments, since those items are reviewed separately by management.

Revenues between segments are accounted for at prices that approximate fair value. These include revenues from the sale of residual fiber from the wood products segment to the pulp segment for use in the pulp production process and from the sale of residual fuel from the pulp segment to the wood products segment for use in energy production.

For the three and nine month periods ended September 30, 2016 there was only one reportable business segment, pulp, as the Friesau Facility was acquired on April 12, 2017. The following table shows information by reportable business segments for the three and nine month periods ended September 30, 2017.

<b>Three Months Ended September 30, 2017</b>	<b>Pulp</b>	<b>Wood Products</b>	<b>Corporate and Other</b>	<b>Elimination Adjustment</b>	<b>Consolidated</b>
Revenues from external customers	\$ 272,358	\$ 33,140	\$	\$	\$ 305,498
Revenues from other segments	\$ 1,056	\$ 5,753	\$	\$ (6,809)	\$
Operating income (loss)	\$ 40,609	\$ 2,983	\$ (2,303)	\$	\$ 41,289
Depreciation and amortization	\$ 21,149	\$ 1,419	\$ 105	\$	\$ 22,673
Purchase of property, plant and equipment	\$ 13,654	\$ 665	\$ 23	\$	\$ 14,342
<b>Nine Months Ended September 30, 2017</b>	<b>Pulp</b>	<b>Wood Products</b>	<b>Corporate and Other</b>	<b>Elimination Adjustment</b>	<b>Consolidated</b>
Revenues from external customers	\$ 781,028	\$ 50,431	\$	\$	\$ 831,459
Revenues from other segments	\$ 1,056	\$ 8,739	\$	\$ (9,795)	\$
Operating income (loss)	\$ 103,302	\$ 3,064	\$ (5,604)	\$	\$ 100,762
Depreciation and amortization	\$ 59,652	\$ 2,553	\$ 314	\$	\$ 62,519
Purchase of property, plant and equipment	\$ 39,714	\$ 2,510	\$ 25	\$	\$ 42,249

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Total assets \$ 1,247,761 \$ 116,522 \$ 21,599 \$ 1,385,882  
 For the three and nine month periods ended September 30, 2016 the Company had a corporate and other operating loss of \$1,491 and \$5,281, respectively.

The pulp segment includes revenues from the sale of pulp and energy and chemical by-products. The wood products segment includes revenues from the sale of lumber and energy and other wood residual by-products. The Company's revenues from external customers by product are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Pulp	\$ 247,314	\$ 215,835	\$ 712,810	\$ 644,519
Lumber	27,851		41,444	
Other wood residuals	2,173		3,226	
Energy and chemical	28,160	22,106	73,979	65,410
Total revenues	\$ 305,498	\$ 237,941	\$ 831,459	\$ 709,929

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**MERCER INTERNATIONAL INC.****NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)**

The following table presents revenues from external customers by geographic area based on location of the customer:

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Germany	\$ 130,943	\$ 101,506	\$ 344,042	\$ 305,078
China	60,604	54,504	194,280	165,550
Other European Union countries	64,907	46,453	171,308	133,039
Italy	12,506	12,686	36,991	42,012
Other Asia	12,648	7,398	38,270	24,201
U.S.	15,734	9,644	26,852	26,427
Other countries	8,156	5,750	19,716	13,622
Total revenues	\$ 305,498	\$ 237,941	\$ 831,459	\$ 709,929

**Note 11. Derivative Transactions**

The Company is exposed to certain market risks relating to its ongoing business. The Company seeks to manage these risks through internal risk management policies as well as, from time to time, the use of derivatives. The derivatives are measured at fair value with changes in fair value immediately recognized in other income (expenses) in the Interim Consolidated Statement of Operations.

**Interest Rate Swaps**

During 2002, the Company entered into certain variable-to-fixed interest rate swaps, referred to as the Stendal Interest Rate Swap Contract in connection with its long-term indebtedness relating to the Stendal mill to fix the interest rate. Under the Stendal Interest Rate Swap Contract, the Company pays a fixed rate and receives a floating rate with the interest payments being calculated on a notional amount. The interest rate swaps were left in place following the refinancing of the debt in November 2014. As at September 30, 2017, the contract had a fair value of 2.6 million (\$3,109; 2016 \$6,522) which was classified as current within accounts payable and other in the Interim Consolidated Balance Sheets. The contract has an aggregate notional amount of 94.3 million, a fixed interest rate of 5.28% and matures in October 2017.

The Company has pledged as collateral cash in the amount of 67% of the fair value of the interest rate swap up to 8.5 million to the derivative counterparty. The calculation to determine the collateral is performed semi-annually, with the final calculation in October 2017. As at September 30, 2017, the collateral was 1.8 million (\$2,125; 2016 \$4,327). This cash has been classified as restricted cash in the Interim Consolidated Balance Sheets.

The counterparty to the interest rate derivative is a bank that is a member of a banking syndicate that holds the Stendal 75.0 million revolving credit facility and the Company does not anticipate non-performance by the bank.

**Credit Risk**

The Company's credit risk is primarily attributable to cash held in bank accounts and accounts receivable. The Company maintains cash balances in foreign financial institutions in excess of insured limits. The Company limits its credit exposure on cash held in bank accounts by periodically investing cash in excess of short-term operating requirements and debt obligations in low risk government bonds, or similar debt instruments. The Company's credit risk associated with the sale of pulp, lumber and other wood residuals is managed through setting credit limits, the purchase of credit insurance and for certain customers a letter of credit is received prior to shipping the product. Concentrations of credit risk on the sale of pulp, lumber and other wood residuals are with customers and agents based primarily in Germany, China and Italy.

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**MERCER INTERNATIONAL INC.**
**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)**

The carrying amount of cash and cash equivalents of \$157,217, restricted cash of \$2,125 and accounts receivable of \$181,062 recorded in the Interim Consolidated Balance Sheets, net of any allowances for losses, represents the Company's maximum exposure to credit risk.

**Note 12. Fair Value Measurement and Disclosure**

Due to their short-term maturity, the carrying amounts of cash and cash equivalents, restricted cash, accounts receivable and accounts payable and other approximates their fair value.

The fair value of the interest rate derivative liability classified as Level 2 was determined using a discounted cash flow model that uses as its basis readily observable market inputs, such as forward interest rates and yield curves observable at specified intervals. The observable inputs reflect market data obtained from independent sources, including the Euribor rate provided by the counterparty to the interest rate derivative.

The fair value of the 2022 Senior Notes, 2024 Senior Notes and 2019 Senior Notes classified as Level 2 was determined using quoted prices in a dealer market, or using recent market transactions.

The following tables present a summary of the Company's outstanding financial instruments and their estimated fair values under the fair value hierarchy:

Description	Fair value measurements as at September 30, 2017 using:					
	Level 1	Level 2	Level 3	Total		
Interest rate derivative liability	\$	\$	3,109	\$	\$	3,109
Debt						
Revolving credit facility			29,515			29,515
2022 Senior Notes and 2024 Senior Notes			685,125			685,125
	\$	\$	717,749	\$	\$	717,749

Description	Fair value measurements as at December 31, 2016 using:					
	Level 1	Level 2	Level 3	Total		
Interest rate derivative liability	\$	\$	6,522	\$	\$	6,522
2019 Senior Notes and 2022 Senior Notes			654,378			654,378
	\$	\$	660,900	\$	\$	660,900

**Note 13. Commitments and Contingencies**

- (a) The Company is involved in legal actions and claims arising in the ordinary course of business. While the outcome of any legal actions and claims cannot be predicted with certainty, it is the opinion of management that the outcome of any such claims which are pending or threatened, either individually or on a combined basis, will not have a material adverse effect on the consolidated financial condition, results of operations or liquidity of the Company.
- (b) The Company is subject to regulations that require the handling and disposal of asbestos in a prescribed manner if a property undergoes a major renovation or demolition. Otherwise, the Company is not required to remove asbestos from its facilities. Generally asbestos is found on steam and condensate piping systems as well as certain cladding on buildings and in building insulation throughout older facilities. The Company's obligation for the proper removal and disposal of asbestos products from the Company's mills is a conditional asset retirement obligation. As a result of the longevity of the Company's mills, due in part to the maintenance procedures and the fact that the Company does not have plans for major changes that require the removal of asbestos, the timing of the asbestos removal is indeterminate. As a result, the Company is currently unable to reasonably estimate the fair value of its asbestos removal and disposal obligation. The Company will recognize a liability in the period in which sufficient information is available to reasonably estimate its fair value.

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### NON-GAAP FINANCIAL MEASURES

This quarterly report on Form 10-Q contains non-GAAP financial measures, that is, financial measures that either exclude or include amounts that are not excluded or included in the most directly comparable measure calculated and presented in accordance with the generally accepted accounting principles in the United States, referred to as GAAP. Specifically, we make use of the non-GAAP measure Operating EBITDA.

Operating EBITDA is defined as operating income (loss) plus depreciation and amortization and non-recurring capital asset impairment charges. We use Operating EBITDA as a benchmark measurement of our own operating results and as a benchmark relative to our competitors. We consider it to be a meaningful supplement to operating income as a performance measure primarily because depreciation expense and non-recurring capital asset impairment charges are not actual cash costs, and depreciation expense varies widely from company to company in a manner that we consider largely independent of the underlying cost efficiency of our operating facilities. In addition, we believe Operating EBITDA is commonly used by securities analysts, investors and other interested parties to evaluate our financial performance.

Operating EBITDA does not reflect the impact of a number of items that affect our net income (loss), including financing costs and the effect of derivative instruments. Operating EBITDA is not a measure of financial performance under GAAP, and should not be considered as an alternative to net income (loss) or income (loss) from operations as a measure of performance, or as an alternative to net cash from operating activities as a measure of liquidity. Operating EBITDA is an internal measure and therefore may not be comparable to other companies.

Operating EBITDA has significant limitations as an analytical tool, and should not be considered in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are that Operating EBITDA does not reflect: (i) our cash expenditures, or future requirements, for capital expenditures or contractual commitments; (ii) changes in, or cash requirements for, working capital needs; (iii) the significant interest expense, or the cash requirements necessary to service interest or principal payments, on our outstanding debt; (iv) the impact of realized or marked to market changes in our derivative positions, which can be substantial; and (v) the impact of impairment charges against our investments or assets. Because of these limitations, Operating EBITDA should only be considered as a supplemental performance measure and should not be considered as a measure of liquidity or cash available to us to invest in the growth of our business. Because all companies do not calculate Operating EBITDA in the same manner, Operating EBITDA as calculated by us may differ from Operating EBITDA or EBITDA as calculated by other companies. We compensate for these limitations by using Operating EBITDA as a supplemental measure of our performance and by relying primarily on our GAAP financial statements.

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In this document: (i) unless the context otherwise requires, references to we, our, us, the Company or Mercer International Inc. and its subsidiaries; (ii) references to Mercer Inc. mean the Company excluding its subsidiaries; (iii) information is provided as of September 30, 2017, unless otherwise stated; (iv) our reporting currency is dollars and references to € mean euros and C\$ mean Canadian dollars; (v) ADMTs refers to air-dried metric tonnes; (vi) MW refers to megawatts and MWh refers to megawatt hours; and (vii) Mfbm refers to thousand board feet.

The following discussion and analysis of our results of operations and financial condition for the three and nine months ended September 30, 2017 should be read in conjunction with our interim consolidated financial statements and related notes included in this quarterly report, as well as our most recent annual report on Form 10-K for the fiscal year ended December 31, 2016 filed with the Securities and Exchange Commission, referred to as the SEC.

### Results of Operations

#### General

Since April 12, 2017, when we acquired substantially all of the assets of one of Germany's largest sawmills and a bio-mass power plant near Friesau, Germany, referred to as the Friesau Facility, for approximately \$61.6 million, we have two reportable operating segments:

- **Pulp** consists of the manufacture, sales and distribution of northern bleached softwood kraft pulp, referred to as NBSK pulp, electricity and other by-products at our three pulp mills with an aggregate annual production capacity of approximately 1.5 million ADMTs of NBSK pulp and 305 MW of electricity.

- **Wood Products** consists of the manufacture, sales and distribution of lumber, electricity and other wood residuals at the Friesau Facility with an annual production capacity of approximately 550 million board feet of lumber and 13 MW of electricity.

Each segment offers primarily different products and requires different manufacturing processes, technology and sales and marketing.

The European and U.S. lumber markets are very different. In the European market, lumber is generally customized in terms of dimensions and finishing, whereas the U.S. market is driven primarily by demand from new housing starts and dimensions and finishing are generally standardized.

Additionally, lumber production and sales in Europe are commonly measured in cubic meters, whereas in the U.S. they are measured in thousand board feet or Mfbm. For the purposes of this report, we have converted our lumber metrics from cubic meters to Mfbm using a conversion ratio of 1.6 cubic meters of lumber equalling a Mfbm of lumber, which is the ratio commonly used in the industry.

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### ***Current Market Environment***

In the third quarter of 2017, pulp prices in Europe and North America increased as a result of continued steady demand and were generally flat in China compared to the prior quarter of 2017. Overall our average pulp sales realizations were approximately 2% higher in the third quarter of 2017 compared to the prior quarter of 2017.

Late in the third quarter of 2017, prices increased in China as a result of strong demand and a sharp reduction in China's imports of recovered or waste paper. Such reduction resulted from a major environmental policy shift announced by China in the third quarter of 2017 to reduce and phase out imports of solid waste and scraps, including recovered or waste paper.

At the end of the current quarter, list prices in Europe, China and North America were approximately \$920, \$710 and \$1,130 per ADMT, respectively. In October 2017, we announced list price increases of \$90 and \$40 per ADMT in China and Europe, respectively. However, we cannot assure that such increases will be fully implemented and, as prices are highly cyclical, that they will not decline in the future.

Currently, the NBSK pulp market is balanced with world producer inventories at about 29 days' supply.

Looking forward, we believe the new pulp production capacity that has or is coming online will not materially adversely impact the market in 2017 as a result of steady demand growth and limited supply and quality of recycled fiber. Further, we expect some of the new capacity will not hit the market in a meaningful amount until 2018. As a result, we currently expect overall steady pulp demand in the near term.

In the last quarter of 2017, our only scheduled annual maintenance downtime is three days at our Stendal mill.

In the third quarter of 2017, we commenced lumber sales into the U.S. market which accounted for approximately 10% of our lumber sales volumes while substantially all the rest were to Europe.

In the third quarter of 2017, U.S. benchmark lumber prices for Western SPF No. 2 and better averaged \$405 per Mfbm. There is no similar or common pricing metric quoted in the European market. In the third quarter of 2017, our average lumber sales realization was \$375 per Mfbm.

Currently both the European and U.S. lumber markets are strong and prices are near multi-year highs and are expected to remain steady in the near term.

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**Summary Financial Highlights**

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
	<b>(in thousands, other than per share amounts)</b>			
Pulp segment revenues	\$ 272,358	\$ 237,941	\$ 781,028	\$ 709,929
Wood products segment revenues	33,140	-	50,431	-
<b>Total revenues</b>	<b>\$ 305,498</b>	<b>\$ 237,941</b>	<b>\$ 831,459</b>	<b>\$ 709,929</b>
Pulp segment operating income	\$ 40,609	\$ 31,312	\$ 103,302	\$ 79,979
Wood products operating income	2,983	-	3,064	-
Corporate and other operating loss	(2,303)	(1,491)	(5,604)	(5,281)
<b>Total operating income</b>	<b>\$ 41,289</b>	<b>\$ 29,821</b>	<b>\$ 100,762</b>	<b>\$ 74,698</b>
Pulp segment depreciation and amortization	\$ 21,149	\$ 17,923	\$ 59,652	\$ 52,810
Wood products depreciation and amortization	1,419	-	2,553	-
Corporate and other depreciation and amortization	105	108	314	402
<b>Total depreciation and amortization</b>	<b>\$ 22,673</b>	<b>\$ 18,031</b>	<b>\$ 62,519</b>	<b>\$ 53,212</b>
Operating EBITDA <sup>(1)</sup>	\$ 63,962	\$ 47,852	\$ 163,281	\$ 127,910
Loss on settlement of debt <sup>(2)</sup>	\$ -	\$ -	\$ 10,696	\$ 454
Income tax provision	\$ 6,632	\$ 5,109	\$ 21,897	\$ 19,181
<b>Net income</b>	<b>\$ 21,143</b>	<b>\$ 11,926</b>	<b>\$ 28,765</b>	<b>\$ 16,454</b>
Net income per common share				
Basic	\$ 0.33	\$ 0.18	\$ 0.44	\$ 0.25
Diluted	\$ 0.32	\$ 0.18	\$ 0.44	\$ 0.25
Common shares outstanding at period end	65,017	64,694	65,017	64,694

(1) The following table provides a reconciliation of net income to operating income and Operating EBITDA for the periods indicated:

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
	<b>(in thousands)</b>			
Net income	\$ 21,143	\$ 11,926	\$ 28,765	\$ 16,454
Income tax provision	6,632	5,109	21,897	19,181
Interest expense	13,513	12,791	40,712	38,718
Loss on settlement of debt	-	-	10,696	454
Other (income) expenses	1	(5)	(1,308)	(109)
<b>Operating income</b>	<b>41,289</b>	<b>29,821</b>	<b>100,762</b>	<b>74,698</b>
<b>Add: Depreciation and amortization</b>	<b>22,673</b>	<b>18,031</b>	<b>62,519</b>	<b>53,212</b>
<b>Operating EBITDA</b>	<b>\$ 63,962</b>	<b>\$ 47,852</b>	<b>\$ 163,281</b>	<b>\$ 127,910</b>



(2) Redemption of 7.0% Senior Notes due 2019.

**Selected Production, Sales and Other Data**

<b>Pulp Segment</b>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Pulp production ( '000 ADMTs)	388.1	361.8	1,124.5	1,078.1
Annual maintenance downtime ( '000 ADMTs)	10.2	10.2	42.7	39.8
Annual maintenance downtime (days)	10	10	32	31
Pulp sales ( '000 ADMTs)	383.8	359.8	1,147.7	1,083.6
Average NBSK pulp list prices in Europe (\$/ADMT) <sup>(1)</sup>	903	810	869	800
Average NBSK pulp list prices in China (\$/ADMT) <sup>(1)</sup>	670	595	662	601
Average NBSK pulp list prices in North America (\$/ADMT) <sup>(1)</sup>	1,110	998	1,079	974
Average pulp sales realizations (\$/ADMT) <sup>(2)</sup>	638	593	615	588
Energy production ( '000 MWh)	497.5	473.8	1,418.5	1,380.8
Energy sales ( '000 MWh)	224.8	208.4	620.9	606.0
Average energy sales realizations (\$/MWh)	97	92	92	90

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<b>Wood Products Segment</b>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Lumber production (million board feet)	109.6	-	177.1	-
Lumber sales (million board feet)	74.2	-	115.7	-
Average lumber sales realizations (\$/Mfbm)	375	-	358	-
Energy sales ( 000 MWh)	24.5	-	48.5	-
Average energy sales realizations (\$/MWh)	127	-	119	-
<b>Average Spot Currency Exchange Rates</b>				
\$ / <sup>(3)</sup>	1.1755	1.1163	1.1146	1.1166
\$ / C\$ <sup>(3)</sup>	0.7984	0.7663	0.7659	0.7578

(1) Source: RISI pricing report.

(2) Sales realizations after customer discounts, rebates and other selling concessions. Incorporates the effect of pulp price variations occurring between the order and shipment dates.

(3) Average Federal Reserve Bank of New York Noon Buying Rates over the reporting period.

***Consolidated - Three Months Ended September 30, 2017 Compared to Three Months Ended September 30, 2016***

Total revenues for the three months ended September 30, 2017 increased by approximately 28% to \$305.5 million from \$237.9 million in the same quarter of 2016 primarily due to the inclusion of \$33.1 million of wood product revenues and 15% higher pulp revenues. In the current quarter, pulp revenues benefitted from an approximately 8% increase in pulp sales realizations and an approximately 7% increase in sales volumes.

Costs and expenses in the current quarter increased by approximately 27% to \$264.2 million from \$208.1 million in the third quarter of 2016 primarily due to the inclusion of costs and expenses from our wood products segment, the negative impact of a weaker dollar on our euro and Canadian dollar denominated costs and expenses and higher pulp sales volumes.

In the third quarter of 2017, operating depreciation and amortization increased to \$22.6 million from \$17.9 million in the same quarter of 2016 due to the completion of large capital projects at our pulp mills and the acquisition of the Friesau Facility.

Selling, general and administrative expenses increased to \$12.3 million in the third quarter of 2017 from \$10.1 million in the same quarter of 2016 primarily due to the inclusion of the wood products segment.

In the third quarter of 2017, our operating income increased by approximately 39% to \$41.3 million from \$29.8 million in the same quarter of 2016 primarily due to higher pulp sales realizations and sales volumes partially offset by the negative impact of a weaker dollar on our euro and Canadian dollar denominated costs and expenses.

Interest expense in the current quarter increased to \$13.5 million from \$12.8 million in the same quarter of 2016 primarily as a result of drawing 25.0 million on our 70.0 million revolving credit facility to partially finance the acquisition of the Friesau Facility and an increase in its working capital resulting from the ramp up of its operations.

During the third quarter of 2017, income tax expense increased to \$6.6 million from \$5.1 million in the same quarter of 2016 due to higher taxable income for our German mills.

For the third quarter of 2017, our net income increased to \$21.1 million, or \$0.33 per basic share and \$0.32 per diluted share, from \$11.9 million, or \$0.18 per basic and diluted share, in the same quarter of 2016.

In the third quarter of 2017, Operating EBITDA increased by approximately 34% to \$64.0 million from \$47.9 million in the same quarter of 2016 primarily due to higher pulp sales realizations and sales volumes and the inclusion of our wood products segment, partially offset by the negative impact of a weaker dollar.

### Operating Results by Business Segment

None of the income or loss items following operating income in our Interim Consolidated Statement of Operations are allocated to our segments, since those items are reviewed separately by management.

### *Pulp Segment - Three Months Ended September 30, 2017 Compared to Three Months Ended September 30, 2016*

#### *Selected Financial Information*

	<b>Three Months Ended September 30, 2017          2016 (in thousands)</b>	
Pulp revenues	\$ 247,314	\$ 215,835
Energy and chemical revenues	\$ 25,044	\$ 22,106
Operating depreciation and amortization	\$ 21,149	\$ 17,923
Operating income	\$ 40,609	\$ 31,312

Pulp revenues in the third quarter of 2017 increased by approximately 15% to \$247.3 million from \$215.8 million in the same quarter of 2016 due to higher sales realizations and sales volumes.

Energy and chemical revenues increased by approximately 13% to \$25.0 million in the third quarter of 2017 from \$22.1 million in the same quarter of 2016 due to record sales volumes.

Pulp production increased by approximately 7% to 388,102 ADMTs, being a quarterly pulp production record, in the current quarter from 361,800 ADMTs in the same quarter of 2016. In the third quarter of 2017 and 2016, we had 10 days (approximately 10,200 ADMTs) of annual maintenance downtime at our Rosenthal mill.

We estimate that annual maintenance downtime in the current quarter adversely impacted our operating income by approximately \$6.8 million, comprised of approximately \$5.2 million in direct out-of-pocket expenses and the balance in reduced production. Many of our competitors that report their financial results using International Financial Reporting Standards ( IFRS ) capitalize their direct costs of maintenance downtime.

Pulp sales volumes increased by approximately 7% to 383,795 ADMTs in the current quarter from 359,791 ADMTs in the same quarter of 2016 primarily due to strong production and continued steady demand in China and Europe.

In the current quarter of 2017, list prices for NBSK pulp in Europe and China increased from the same quarter of 2016, largely as a result of overall steady demand. Average list prices for NBSK pulp in Europe were approximately \$903 per ADMT in the third quarter of 2017, compared to approximately \$810 per ADMT in the same quarter of 2016. Average list prices for NBSK pulp in China and North America were approximately \$670 per ADMT and \$1,110 per ADMT, respectively, in the current quarter, compared to approximately \$595 per ADMT and \$998 per ADMT, respectively, in the same quarter of 2016.

In the third quarter of 2017, as part of achieving the goals of its next five-year plan, China announced a major policy shift to enhance green development by sharply reducing the imports of waste/scrap materials including recovered or waste paper. In the current quarter, China announced goals to stop imports of unsorted paper by the start of 2018 and all solid waste and scrap imports by the end of 2019.

It is too early to predict how China's new policies will evolve, be implemented and their full effect. However, a material reduction in Chinese imports of waste or unsorted paper is expected to increase pulp demand in China over the medium term.

Average pulp sales realizations increased by approximately 8% to \$638 per ADMT in the third quarter of 2017 from approximately \$593 per ADMT in the same quarter of 2016 primarily due to higher list prices.

Compared to the same quarter of the prior year the dollar was weaker against the euro and Canadian dollar which increased the cost of our euro and Canadian dollar costs and expenses and contributed to a negative foreign exchange impact on operating income of approximately \$13.7 million when compared to the same quarter of the prior year.

Costs and expenses for our pulp segment in the current quarter increased by approximately 13% to \$232.8 million from \$206.6 million in the third quarter of 2016 primarily due to the negative impact of a weaker dollar on our euro and Canadian dollar denominated costs and expenses and higher pulp sales volumes.

In the third quarter of 2017, pulp segment operating depreciation and amortization increased to \$21.1 million from \$17.9 million in the same quarter of 2016 primarily due the acquisition of customized rail cars for our German mills and the completion of other large capital projects.

On average, in the current quarter overall per unit fiber costs increased by approximately 5% from the same quarter of 2016 primarily as a result of the weaker dollar on our euro and Canadian dollar denominated fiber costs. The fiber markets in both Germany and in the Celgar mill's fiber basket continued to be balanced. In the current quarter, per unit fiber costs in Germany were approximately 9% higher than the comparative quarter and for our Celgar mill were approximately 3% lower than the comparative quarter.

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Transportation costs for our pulp segment increased by approximately 11% to \$19.4 million in the current quarter from \$17.5 million in the same quarter of 2016 primarily due to higher sales volumes.

In the third quarter of 2017, we entered into a new collective agreement with employees at our Rosenthal mill which expires in February 2019 and provides for a 2.4% annual wage increase on July 1, 2017 and a further 1.2% increase on August 1, 2018.

In the third quarter of 2017, pulp segment operating income increased by approximately 30% to \$40.6 million from \$31.3 million in the same quarter of 2016 primarily due to higher pulp sales realizations and sales volumes partially offset by the net impact of a weaker dollar.

### *Wood Products Segment - Three Months Ended September 30, 2017*

#### *Selected Financial Information*

	<b>Three Months Ended September 30, 2017 (in thousands)</b>
Lumber revenues	\$ 27,851
Energy revenues	\$ 3,116
Other wood residual revenues	\$ 2,173
Operating depreciation and amortization	\$ 1,419
Operating income	\$ 2,983

On April 12, 2017, we entered into the wood products business with the acquisition of the Friesau Facility.

In the third quarter of 2017, lumber revenues were \$27.9 million, of which approximately 10% of sales volumes were in the U.S. market and substantially all remaining sales were in Europe. Depending on market conditions, we currently intend to increase our lumber sales to the U.S. market to up to half of the lumber production from Friesau. European and U.S. lumber markets were generally strong and prices steady and near multi-year highs.

In the third quarter of 2017, we produced 109.6 million board feet of lumber. Lumber sales volumes were 74.2 million board feet as we completed our inventory build-up to support sales to the U.S. market, some of which sales will be realized in the last quarter of 2017. In the current quarter, our average lumber sales realization was \$375 per Mfbm.

In the third quarter, energy and other by-product revenues were approximately \$5.3 million.

Our fiber costs were approximately 80% of our cash production costs. The ramping up of production since acquisition resulted in our purchasing large volumes of sawlogs in a short period. This resulted in our sawlog costs being marginally higher than our regional competitors. We currently expect our sawlog costs to remain flat in the fourth quarter of 2017 and to compare more favorably to regional competitors in 2018.

In the current quarter we continued to realize upon fiber synergies between the Friesau Facility and our Rosenthal pulp mill. During the current quarter, the facility shipped approximately 291,800 cubic meters of chips to Rosenthal, and Rosenthal has shipped approximately 19,900



cubic meters of waste wood to Friesau. Both volumes are in line with our forecasts and have begun to lower costs at both mills.

In the third quarter of 2017, operating depreciation and amortization for our wood products segment was \$1.4 million.

In the third quarter of 2017, our wood products segment operating income was \$3.0 million.

***Consolidated - Nine Months Ended September 30, 2017 Compared to Nine Months Ended September 30, 2016***

Total revenues for the nine months ended September 30, 2017 increased by approximately 17% to \$831.5 million from \$709.9 million in the same period of 2016 primarily due to higher pulp revenues and \$50.4 million of wood products revenue.

Costs and expenses in the nine months ended September 30, 2017 increased by approximately 15% to \$730.7 million from \$635.2 million in the same period of 2016 primarily due to the inclusion of our wood products segment and higher pulp sales volumes.

In the nine months ended September 30, 2017, operating depreciation and amortization increased to \$62.2 million from \$52.8 million in the same period of 2016 due to completion of large capital projects at our pulp mills and the acquisition of the Friesau Facility.

Selling, general and administrative expenses increased to \$35.3 million in the nine months ended September 30, 2017 from \$32.1 million in the same period of 2016 primarily due to the inclusion of our wood products segment.

In the nine months ended September 30, 2017, our operating income increased by approximately 35% to \$100.8 million from \$74.7 million in the same period of 2016 primarily due to higher pulp sales realizations.

In the nine months ended September 30, 2017, we issued, in two tranches, an aggregate \$250.0 million of 6.5% senior notes due 2024, referred to as the 2024 Senior Notes . We utilized the proceeds primarily to redeem \$227.0 million of our 7.0% senior notes due 2019, referred to as the 2019 Senior Notes , at a cost, including premium, of \$234.9 million and recorded a loss on such redemption of \$10.7 million (being \$0.16 per basic and diluted share).

Interest expense in the nine months ended September 30, 2017 increased to \$40.7 million from \$38.7 million in the same period of 2016, since, during the requisite notice period for redemption of the 2019 Senior Notes, we also had \$225.0 million of the 2024 Senior Notes outstanding.

During the nine months ended September 30, 2017, income tax expense increased to \$21.9 million from \$19.2 million in the same period of 2016 due to higher taxable income for our German mills.

For the nine months ended September 30, 2017, net income increased to \$28.8 million, or \$0.44 per basic and diluted share, from \$16.5 million, or \$0.25 per basic and diluted share, in the same period of 2016.

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In the nine months ended September 30, 2017, Operating EBITDA increased by approximately 28% to \$163.3 million from \$127.9 million in the same period of 2016 primarily as a result of higher pulp sales realizations and, to a lesser degree, the inclusion of our wood products segment.

***Pulp Segment - Nine Months Ended September 30, 2017 Compared to Nine Months Ended September 30, 2016***

***Selected Financial Information***

	<b>Nine Months Ended September 30, 2017                  2016 (in thousands)</b>	
Pulp revenues	\$ 712,810	\$ 644,519
Energy and chemical revenues	\$ 68,218	\$ 65,410
Operating depreciation and amortization	\$ 59,652	\$ 52,810
Operating income	\$ 103,302	\$ 79,979

Pulp revenues in the nine months ended September 30, 2017 increased by approximately 11% to \$712.8 million from \$644.5 million in the same period of 2016 due to higher sales volumes and sales realizations.

Energy and chemical revenues increased by approximately 4% to \$68.2 million in the nine months ended September 30, 2017 compared to \$65.4 million in the same period of 2016 primarily due to higher sales volumes.

Pulp production increased to 1,124,532 ADMTs in the nine months ended September 30, 2017 from 1,078,057 ADMTs in the same period of 2016. In the nine months ended September 30, 2017, we had annual maintenance downtime of 32 days (approximately 42,700 ADMTs), compared to 31 days (approximately 39,800 ADMTs) in the same period of 2016.

We estimate that such maintenance downtime in the nine months ended September 30, 2017 adversely impacted our operating income by approximately \$34.3 million, comprised of approximately \$26.3 million in direct out-of-pocket expenses and the balance in reduced production. Many of our competitors that report their financial results using IFRS capitalize their direct costs of maintenance downtime.

Pulp sales volumes increased to 1,147,691 ADMTs in the nine months ended September 30, 2017 compared to 1,083,570 ADMTs in the same period of 2016 primarily due to continued steady demand from both China and Europe and strong production.

In the nine months ended September 30, 2017, list prices for NBSK pulp increased from the same period of 2016, largely as a result of continued steady demand. Average list prices for NBSK pulp in Europe were approximately \$869 per ADMT in the nine months ended September 30, 2017, compared to approximately \$800 per ADMT in the same period of 2016. Average list prices for NBSK pulp in China and North America were approximately \$662 per ADMT and \$1,079 per ADMT, respectively, in the nine months ended September 30, 2017, compared to approximately \$601 per ADMT and \$974 per ADMT, respectively, in the same period of 2016.

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Average pulp sales realizations increased by approximately 5% to \$615 per ADMT in the nine months ended September 30, 2017 from approximately \$588 per ADMT in the same period last year primarily due to higher list prices.

At the end of the nine months ended September 30, 2017, the dollar weakened against the euro which reduced our dollar denominated cash and receivables held by our German pulp mills and contributed to a negative foreign exchange impact on operating income of approximately \$8.0 million when compared to the same period of the prior year.

Costs and expenses in the nine months ended September 30, 2017 increased by approximately 8% to \$678.8 million from \$630.0 million in the nine months ended September 30, 2016 primarily due to higher sales volumes, higher maintenance costs and the reversal in 2016 of an accrual for wastewater fees at our Rosenthal mill of \$7.2 million.

In the nine months ended September 30, 2017, operating depreciation and amortization increased to \$59.7 million from \$52.8 million in the same period of 2016 due to the completion of several major capital projects.

On average, in the nine months ended September 30, 2017 overall per unit fiber prices decreased by approximately 3% from the same period of 2016 primarily as a result of a balanced wood market in both Germany and the Celgar mill's fiber basket. In the nine months ended September 30, 2017 average per unit fiber prices in Germany were approximately 2% lower than the comparative period. In the nine months ended September 30, 2017 average per unit fiber prices for our Celgar mill were approximately 3% lower than the comparative period.

Transportation costs increased by approximately 12% to \$56.9 million in the nine months ended September 30, 2017 from \$50.8 million in the same period of 2016 primarily due to higher sales volumes.

In the nine months ended September 30, 2017, pulp segment operating income increased by approximately 29% to \$103.3 million from \$80.0 million in the same period of 2016 primarily due to higher pulp sales realizations and sales volumes, partially offset by the negative impact of a weaker dollar, higher maintenance costs and the reversal in 2016 of an accrual for wastewater fees.

### *Wood Products Segment - Nine Months Ended September 30, 2017*

#### *Selected Financial Information*

	<b>Nine Months Ended September 30, 2017 (in thousands)</b>
Lumber revenues	\$ 41,444
Energy revenues	\$ 5,761
Other wood residual revenues	\$ 3,226
Operating depreciation and amortization	\$ 2,553
Operating income	\$ 3,064

We entered into the wood products business with the acquisition of the Friesau Facility on April 12, 2017. As a result, our results for the nine months ended September 30, 2017 commence at the acquisition date.

In the nine months ended September 30, 2017, we had lumber revenues of \$41.4 million, substantially all of which were in the European market. European lumber markets were generally strong and prices steady and near multi-year highs.

We produced 177.1 million board feet of lumber. Lumber sales volumes were 115.7 million board feet as we continued to build inventory to support sales to the U.S. market. In the nine months ended September 30, 2017, our average lumber sales realization was \$358 per Mfbm.

In the nine months ended September 30, 2017, energy and other by-product revenues were approximately \$9.0 million and we sold 48.5 thousand MWh of electricity.

Our fiber costs were approximately 80% of our cash production costs. The ramping up of production resulted in our purchasing large volumes of sawlogs in a short period. This resulted in our sawlog costs being marginally higher than our regional competitors.

In the nine months ended September 30, 2017 we started realizing on identified fiber synergies between the Friesau Facility and our Rosenthal pulp mill. During the nine months ended September 30, 2017, the facility shipped approximately 471,600 cubic meters of chips to Rosenthal, and Rosenthal has shipped approximately 43,900 cubic meters of waste wood to Friesau. Both volumes are in line with our forecasts and have begun to lower costs at both mills. As at September 30, 2017, we estimate we have realized approximately \$4.8 million of our expected synergy savings.

In the nine months ended September 30, 2017, operating depreciation and amortization for our wood products segment was \$2.6 million.

In the nine months ended September 30, 2017, our wood products segment operating income was \$3.1 million.

## Liquidity and Capital Resources

### Summary of Cash Flows

	Nine Months Ended September 30,	
	2017	2016
	(in thousands)	
Net cash from operating activities	\$ 103,257	\$ 111,179
Net cash used in investing activities	(104,979)	(30,052)
Net cash from (used in) financing activities	9,839	(44,145)
Effect of exchange rate changes on cash, cash equivalents		
and restricted cash	10,329	3,539
Net increase in cash, cash equivalents and restricted cash	\$ 18,446	\$ 40,521

**Cash Flows from Operating Activities.** We operate in a cyclical industry and our operating cash flows vary accordingly. Our principal operating cash expenditures are for labor, fiber and chemicals.

Working capital levels fluctuate throughout the year and are affected by maintenance downtime, changing sales patterns, seasonality and the timing of receivables and sales and the payment of payables and expenses.

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Cash provided by operating activities was \$103.3 million in the nine months ended September 30, 2017 and \$111.2 million in the comparative period of 2016. An increase in accounts receivable used cash of \$42.1 million in the nine months ended September 30, 2017 of which \$10.2 million was related to our wood products segment. In the same period of 2016, a decrease in accounts receivable provided cash of \$9.0 million. An increase in accounts payable and accrued expenses provided cash of \$41.9 million in the nine months ended September 30, 2017 of which \$21.2 million was related to our wood products segment, compared to an increase in accounts payable and accrued expenses providing cash of \$11.9 million in the same period of 2016. An overall increase in inventories used cash of \$9.9 million in the nine months ended September 30, 2017, which reflected an increase of \$27.9 million from our wood products segment and a decrease of \$18.0 in our pulp segment. A decrease in inventories provided cash of \$3.3 million in the comparative period of 2016.

**Cash Flows from Investing Activities.** Investing activities in the nine months ended September 30, 2017 used cash of \$105.0 million primarily related to the acquisition of our Friesau Facility for \$61.6 million and capital expenditures of \$42.2 million. In the nine months ended September 30, 2017, capital expenditures primarily related to a rail acceptance system for logs and additional land for raw material storage at our Rosenthal mill, a pre-bleach press system upgrade and large maintenance projects at our Celgar mill and various other smaller projects. In the same period of 2016, investing activities used cash of \$30.1 million.

**Cash Flows from Financing Activities.** In the nine months ended September 30, 2017, financing activities provided cash of \$9.8 million, including an aggregate of \$250.0 million from the issuance of the 2024 Senior Notes, which was primarily used to redeem the 2019 Senior Notes at a cost of \$234.9 million. In the nine months ended September 30, 2017, debt issuance costs primarily for the 2024 Senior Notes used cash of \$6.1 million, dividend payments used cash of \$22.4 million and a scheduled payment in respect of our interest rate derivative used cash of \$3.8 million. In the nine months ended September 30, 2017, we also drew \$26.5 million on a revolving credit facility to partially finance the acquisition of the Friesau Facility and to build the working capital associated with its ramp up of operations. In the same period of 2016, financing activities used cash of \$44.1 million, including \$23.1 million to repurchase and cancel \$23.0 million of our 2019 Senior Notes, \$22.3 million for the payment of dividends and \$5.9 million for a scheduled payment in respect of our interest rate derivative, partially offset by \$7.7 million of borrowings on our Celgar revolving credit facility.

## Balance Sheet Data

The following table is a summary of selected financial information as at the dates indicated:

	September 30, 2017	December 31, 2016
	(in thousands)	
<b>Financial Position</b>		
Cash and cash equivalents	\$ 157,217	\$ 136,569
Working capital	\$ 370,289	\$ 308,681
Total assets	\$ 1,385,882	\$ 1,158,708
Long term liabilities	\$ 744,565	\$ 686,410
Total equity	\$ 498,001	\$ 379,128

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As a result of the weakening of the dollar versus the euro and the Canadian dollar as at September 30, 2017, we recorded a non-cash increase in the carrying value of our net assets, consisting primarily of our fixed assets, denominated in euros and Canadian dollars. This non-cash increase of approximately \$107.6 million does not affect our net income, Operating EBITDA or cash flows but is reflected in our other comprehensive income and as an increase to our total equity.

### Sources and Uses of Funds

Our principal sources of funds are cash flows from operations, cash and cash equivalents on hand and our revolving credit facilities. Our principal uses of funds consist of operating expenses, capital expenditures and semi-annual interest payments on our outstanding 7.75% Senior Notes due 2022 and our 2024 Senior Notes.

The following table sets out our total capital expenditures and interest expense for the periods indicated:

	<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>
	<b>(in thousands)</b>	
Capital expenditures	\$ 42,249	\$ 28,977
Cash paid for interest <sup>(1)</sup>	\$ 29,311	\$ 26,031
Interest expense <sup>(2)</sup>	\$ 40,712	\$ 38,718

(1) Amounts differ from interest expense which includes non-cash items. See supplemental disclosure of cash flow information from our Interim Consolidated Statements of Cash Flows included in this report.

(2) Interest on our 2022 Senior Notes is paid semi-annually in June and December of each year and interest on our 2024 Senior Notes is paid semi-annually in February and August of each year.

In the nine months ended September 30, 2017, we expended \$22.4 million to pay three quarterly dividends of \$0.115 per common share.

As at September 30, 2017, our cash and cash equivalents increased to \$157.2 million from \$136.6 million at the end of 2016.

As at September 30, 2017, we had approximately \$164.5 million available under our revolving credit facilities.

As at September 30, 2017, we had no material commitments to acquire assets or operating businesses.

Based upon the current level of operations and our current expectations for future periods in light of the current economic environment, and in particular, current and expected pulp and lumber pricing and foreign exchange rates, we believe that cash flow from operations and available cash, together with available borrowings under our revolving credit facilities, will be adequate to finance the capital requirements for our business including the payment of our quarterly dividend during the next 12 months.

In the future we may make acquisitions of businesses or assets or commitments to additional capital projects. To achieve the long-term goals of expanding our assets and earnings, including through acquisitions, capital resources will be required. Depending on the size of a transaction, the capital resources that will be required can be substantial. The necessary resources will be



generated from cash flow from operations, cash on hand, borrowing against our assets or the issuance of securities.

### **Debt Covenants**

Certain of our long-term obligations contain various financial tests and covenants customary to these types of arrangements. See our annual report on Form 10-K for the fiscal year ended December 31, 2016.

As at September 30, 2017, we were in full compliance with all of the covenants of our indebtedness.

### **Off-Balance Sheet Arrangements**

At September 30, 2017, we did not have any off-balance sheet arrangements (as defined in Item 303(a)(4)(ii) of Regulation S-K).

### **Contractual Obligations and Commitments**

There were no material changes outside the ordinary course to any of our material contractual obligations during the nine months ended September 30, 2017.

### **Foreign Currency**

As a majority of our assets, liabilities and expenditures are held or denominated in euros or Canadian dollars, our consolidated financial results are subject to foreign currency exchange rate fluctuations.

We translate foreign denominated assets and liabilities into dollars at the rate of exchange on the balance sheet date. Equity accounts are translated using historical exchange rates. Unrealized gains or losses from these translations are recorded in other comprehensive income (loss) and do not affect our net earnings.

As a result of the weakening of the dollar versus the euro and Canadian dollar as at September 30, 2017, we recorded a non-cash increase of \$107.6 million in the carrying value of our net assets, consisting primarily of our fixed assets, denominated in euros and Canadian dollars. As a result, our accumulated other comprehensive loss decreased to \$76.7 million.

Based upon the exchange rate as at September 30, 2017, the dollar has weakened by approximately 12% and 8% in value against the euro and the Canadian dollar, respectively, since December 31, 2016. See [Quantitative and Qualitative Disclosures about Market Risk](#) .

### **Critical Accounting Policies**

The preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect both the amount and the timing of the recording of assets, liabilities, revenues, and expenses in the consolidated financial statements and accompanying note disclosures. Our management routinely makes judgments and estimates about the effects of matters that are inherently uncertain. As the number of variables and assumptions

affecting the probable future resolution of the uncertainties increases, these judgments become even more subjective and complex.

Our significant accounting policies are disclosed in Note 1 to our audited annual financial statements included in our annual report on Form 10-K for the fiscal year ended December 31, 2016. While all of the significant accounting policies are important to the consolidated financial statements, some of these policies may be viewed as having a high degree of judgment. On an ongoing basis using currently available information, management reviews its estimates, including those related to accounting for, among other things, pension and other post-retirement benefit obligations, deferred income taxes (valuation allowance and permanent reinvestment), depreciation and amortization, future cash flows associated with impairment testing for long-lived assets, the allocation of the purchase price in a business combination to the assets acquired and liabilities assumed, legal liabilities and contingencies. Actual results could differ materially from these estimates, and changes in these estimates are recorded when known.

We have identified certain accounting policies that are the most important to the portrayal of our current financial condition and results of operations.

For information about both our significant and critical accounting policies, see our annual report on Form 10-K for the fiscal year ended December 31, 2016.

#### **Cautionary Statement Regarding Forward-Looking Information**

The statements in this report that are not reported financial results or other historical information are forward-looking statements within the meaning of the *Private Securities Litigation Reform Act of 1995*, as amended.

Generally, forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. They often include words such as expects, anticipates, intends, plans, believes, seeks, or words of similar meaning, or future or conditional verbs, such as will, should, could, or may, although not all forward-looking statements contain these identifying words. Forward-looking statements are based on expectations, forecasts and assumptions by our management and involve a number of risks, uncertainties and other factors, many of which are beyond our control, that could cause actual conditions, events or results to differ significantly from those described in the forward-looking statements. These factors include, but are not limited to, the following:

- our business is highly cyclical;
- a weakening of the global economy, including capital and credit markets, could adversely affect our business and financial results and have a material adverse effect on our liquidity and capital resources;
- our level of indebtedness could negatively impact our financial condition, results of operations and liquidity;
- cyclical fluctuations in the price and supply of our raw materials, particularly fiber, could adversely affect our business;
- we face intense competition in our markets;



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- we are exposed to currency exchange rate fluctuations;
- we are subject to extensive environmental regulation and we could incur substantial costs as a result of compliance with, violations of or liabilities under applicable environmental laws and regulations;
- our business is subject to risks associated with climate change and social and government responses thereto;
- our operations require substantial capital and we may be unable to maintain adequate capital resources to provide for such capital requirements;
- future acquisitions, including our recent acquisition of the Friesau Facility, may result in additional risks and uncertainties in our business;
- fluctuations in prices and demand for lumber could adversely affect our business;
- adverse housing market conditions may increase the credit risk from customers of our Friesau Facility;
- our Friesau Facility's lumber products are vulnerable to declines in demand due to competing technologies or materials;
- changes in credit ratings issued by nationally recognized statistical rating organizations could adversely affect our cost of financing and have an adverse effect on the market price of our securities;
- we rely on government grants and participate in German statutory energy programs;
- we are subject to risks related to our employees;
- we are dependent on key personnel;
- we may experience material disruptions to our production (including as a result of, among other things, planned and unplanned maintenance downtime);
- if our long-lived assets become impaired, we may be required to record non-cash impairment charges that could have a material impact on our results of operations;

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- we may incur losses as a result of unforeseen or catastrophic events, including the emergence of a pandemic, terrorist attacks or natural disasters;
- our insurance coverage may not be adequate;
- we rely on third parties for transportation services;
- our new enterprise resource planning system may cost more than expected, be delayed, fail to perform as planned and interrupt operational transactions during and following the implementation, which could adversely affect our operations and results of operations;
- we periodically use derivatives to manage certain risks which has caused significant fluctuations in our operating results;
- failures or security breaches of our information technology systems could disrupt our operations and negatively impact our business;
- the price of our common stock may be volatile;

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- a small number of our shareholders could significantly influence our business;

- our international sales and operations are subject to applicable laws relating to trade, export controls and foreign corrupt practices, the violation of which could adversely affect our operations; and

- we are exposed to interest rate fluctuations.

Given these uncertainties, you should not place undue reliance on our forward-looking statements. The forgoing review of important factors is not exhaustive or necessarily in order of importance and should be read in conjunction with the risks and assumptions including those set forth in reports and other documents we have filed with or furnished to the SEC, including in our annual report on Form 10-K for the fiscal year ended December 31, 2016. We advise you that these cautionary remarks expressly qualify in their entirety all forward-looking statements attributable to us or persons acting on our behalf. Unless required by law, we do not assume any obligation to update forward-looking statements based on unanticipated events or changed expectations. However, you should carefully review the reports and other documents we file from time to time with the SEC.

## **Cyclical Nature of Business**

### ***Revenues***

The pulp and lumber businesses are highly cyclical in nature and markets are characterized by periods of supply and demand imbalance, which in turn can materially affect prices. Pulp and lumber markets are sensitive to cyclical changes in the global economy, industry capacity and foreign exchange rates, all of which can have a significant influence on selling prices and our operating results. The length and magnitude of industry cycles have varied over time but generally reflect changes in macro-economic conditions and levels of industry capacity. Pulp and lumber are commodities that are generally available from other producers. Because commodity products have few distinguishing qualities from producer to producer, competition is generally based upon price, which is generally determined by supply relative to demand.

Industry capacity can fluctuate as changing industry conditions can influence producers to idle production capacity or permanently close mills. In addition, to avoid substantial cash costs in idling or closing a mill, some producers will choose to operate at a loss, sometimes even a cash loss, which can prolong weak pricing environments due to oversupply. Oversupply of our products can also result from producers introducing new capacity in response to favorable pricing trends. Certain integrated pulp and paper producers have the ability to discontinue paper production by idling their paper machines and selling their NBSK pulp production on the market, if market conditions, prices and trends warrant such actions.

Demand for each of pulp and lumber has historically been determined primarily by general global macro-economic conditions and has been closely tied to overall business activity. NBSK pulp prices have been and are likely to continue to be volatile and can fluctuate widely over time. Between 2007 and 2016, European list prices for NBSK pulp have fluctuated between a low of approximately \$575 per ADMT in 2009 to a high of \$1,030 per ADMT in 2011.

Our mills and operations voluntarily subject themselves to third-party certification as to compliance with internationally recognized, sustainable management standards because end use



paper and lumber customers have shown an increased interest in understanding the origin of products they purchase. Demand for our products could be adversely affected if we, or our suppliers, are unable to achieve compliance, or are perceived by the public as failing to comply, with these standards or if our customers require compliance with alternate standards for which our operations are not certified.

A producer's actual sales price realizations are list prices net of customer discounts, rebates and other selling concessions. Over the last three years, these have increased as producers compete for customers and sales. Our sales price realizations may also be affected by NBSK pulp price movements between the order and shipment dates.

Accordingly, prices for pulp and lumber are driven by many factors outside our control, and we have little influence over the timing and extent of price changes, which are often volatile. Because market conditions beyond our control determine the prices for pulp and lumber, prices may fall below our cash production costs, requiring us to either incur short-term losses on product sales or cease production at one or more of our mills. Therefore, our profitability depends on managing our cost structure, particularly raw materials which represent a significant component of our operating costs and can fluctuate based upon factors beyond our control. If the prices of our products decline, or if prices for our raw materials increase, or both, our results of operations and cash flows could be materially adversely affected.

### *Costs*

Our production costs are influenced by the availability and cost of raw materials, energy and labor, and our plant efficiencies and productivity. Our main raw material is fiber in the form of wood chips, pulp logs and sawlogs. Wood chip, pulp log and sawlog costs are primarily affected by the supply of, and demand for, lumber and pulp, which are both highly cyclical. Higher fiber prices could affect producer profit margins if they are unable to pass along price increases to pulp and lumber customers or purchasers of surplus energy.

### *Currency*

We have manufacturing operations in Germany and Canada. Most of the operating costs and expenses of our German mills are incurred in euros and those of our Celgar mill in Canadian dollars. However, the majority of our sales are in products quoted in dollars. Our results of operations and financial condition are reported in dollars. As a result, our costs generally benefit from a strengthening dollar but are adversely affected by a decrease in the value of the dollar relative to the euro and to the Canadian dollar. Such declines in the dollar relative to the euro and the Canadian dollar reduce our operating margins and the cash flow available to fund our operations and to service our debt. This could have a material adverse effect on our business, financial condition, results of operations and cash flows.

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**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risks from changes in interest rates and foreign currency exchange rates, particularly the exchange rates between the U.S. dollar and the euro and Canadian dollar. Changes in these rates may affect our results of operations and financial condition and, consequently, our fair value. We seek to manage these risks through internal risk management policies as well as the periodic use of derivatives.

For additional information, please refer to Part II, Item 7A. Quantitative and Qualitative Disclosures about Market Risk included in our annual report on Form 10-K for the fiscal year ended December 31, 2016.

During the nine months ended September 30, 2017, we recorded \$nil on our outstanding interest rate derivative, compared to a derivative loss of approximately \$0.3 million in the same period of 2016.

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## **ITEM 4. CONTROLS AND PROCEDURES**

### **Disclosure Controls and Procedures**

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the *Securities Exchange Act of 1934*, as amended, referred to as the Exchange Act ), as of the end of the period covered by this report. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Based on such evaluation, our principal executive officer and principal financial officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act.

It should be noted that any system of controls is based in part upon certain assumptions designed to obtain reasonable (and not absolute) assurance as to its effectiveness and there can be no assurance that any design will succeed in achieving its stated goals.

### **Changes in Internal Controls**

There have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

We are subject to routine litigation incidental to our business, including that which is described in our latest annual report on Form 10-K for the fiscal year ended December 31, 2016. We do not believe that the outcome of such litigation will have a material adverse effect on our business or financial condition.

**ITEM 1A. RISK FACTORS**

Other than as set forth below, there have been no material changes to the factors disclosed in Item 1A. Risk Factors in our annual report on Form 10-K for the fiscal year ended December 31, 2016.

On April 12, 2017, we completed our acquisition of the Friesau Facility. In addition to the operational, economic and other risk factors of a general nature disclosed in our annual report on Form 10-K for the fiscal year ended December 31, 2016, the risk factors respecting our operations disclosed under the following headings under Item 1A. Risk Factors in our annual report on Form 10-K for the fiscal year ended December 31, 2016 are applicable to our Friesau Facility: (i) Our business is highly cyclical in nature ; (ii) A weakening of the global economy, including capital and credit markets, could adversely affect our business and financial results and have a material adverse effect on our liquidity and capital resources ; (iii) Cyclical fluctuations in the price and supply of our raw materials, particularly fiber, could adversely affect our business ; (iv) We face intense competition in our markets ; (v) We rely on government grants and participate in German statutory energy programs ; and (vi) We rely on third parties for transportation services . References in such risk factors to our pulp mills and their operations, including their products and raw materials should be read to apply to the Friesau Facility and its operations, including, product pricing, costs and the availability of sawlogs.

The following additional risk factors are applicable to our Friesau Facility:

***Fluctuations in prices and demand for lumber could adversely affect our business.***

The financial performance of the Friesau Facility depends on the demand for and selling price of lumber, which is subject to significant fluctuations. The markets for lumber are highly volatile and are affected by economic conditions in Europe and Asia, the strength of housing markets in such regions, the growing importance of the Asian market, changes in industry production capacity, changes in inventory levels and other factors beyond our control. Additionally, interest rates have a significant impact on residential construction and renovation activity, which in turn influence the demand for and price of lumber.

***Adverse housing market conditions may increase the credit risk from customers of our Friesau Facility.***

Our Friesau Facility generally extends credit to customers who are generally susceptible to the same economic business risks that we are. Unfavorable housing market conditions could result in financial failures of one or more of such customers. If such customers financial position

becomes impaired, our ability to fully collect receivables from such customers could be impaired and negatively affect our operating results, cash flow and liquidity.

*Our Friesau Facility's lumber products are vulnerable to declines in demand due to competing technologies or materials.*

Our lumber products may compete with alternative products. For example, plastic, wood/plastic or composite materials may be used by builders as alternatives to the lumber products produced by our Friesau Facility. Changes in the prices for oil, chemicals and other products can change the competitive position of our Friesau Facility's lumber products relative to available alternatives and could increase substitution of those products for our Friesau Facility's products. If use of these alternative products grows, demand for and pricing of our Friesau Facility's products could be adversely affected.

**ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURES**

None.

**ITEM 5. OTHER INFORMATION**

None.

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**ITEM 6. EXHIBITS**

<b>Exhibit No.</b>	<b>Description</b>
31.1	<u>Section 302 Certification of Chief Executive Officer</u>
31.2	<u>Section 302 Certification of Chief Financial Officer</u>
32.1*	<u>Section 906 Certification of Chief Executive Officer</u>
32.2*	<u>Section 906 Certification of Chief Financial Officer</u>
101	The following financial statements from the Company's Form 10-Q for the fiscal period ended September 30, 2017, formatted in XBRL: (i) Interim Consolidated Statements of Operations; (ii) Interim Consolidated Statements of Comprehensive Income; (iii) Interim Consolidated Balance Sheets; (iv) Interim Consolidated Statements of Cash Flows; and (v) Notes to Interim Consolidated Financial Statements.

\* In accordance with Release No. 33-8212 of the SEC, these Certifications: (i) are furnished to the SEC and are not filed for the purposes of liability under the Securities Exchange Act of 1934, as amended; and (ii) are not to be subject to automatic incorporation by reference into any of the Company's registration statements filed under the Securities Act of 1933, as amended, for the purposes of liability thereunder or any offering memorandum, unless the Company specifically incorporates them by reference therein.

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