

# Second Quarter Report | 2001

Six months ended June 30



**ABITIBI  
CONSOLIDATED**



## \$108 Million Net Earnings in Second Quarter

Abitibi-Consolidated Inc. reported net earnings of \$108 million in the second quarter ended June 30, 2001. This represents an improvement in net earnings of \$47 million or 77% compared to the same three months in 2000.

Net earnings for the six-month period ended June 30, 2001 amounted to \$240 million compared to \$112 million in the same period of 2000.

On an earnings per share basis, the Company realized \$0.25 for the second quarter of 2001 and \$0.55 for the six-month period ended June 30, 2001 on a weighted average number of shares outstanding of 440 million. This compares to \$0.15 per share on 404 million shares and \$0.34 per share on 327 million shares, respectively, for the same periods in 2000.

The results of Abitibi-Consolidated Inc. reflect the acquisition of Donohue Inc. on April 18, 2000 and the application of the reverse take-over accounting method in which Donohue is considered as the acquirer and, accordingly, all figures prior to April 18, 2000 are the former Donohue results only.

The improvement to earnings in the first half of the year resulted mainly from higher prices in newsprint and value-added papers and from synergies achieved from the acquisition of Donohue. Prices for pulp were lower than in the same period of last year. Higher fibre and energy costs, as well as paper production curtailments during the second quarter of 2001, partially offset the positive impact of higher prices.

The expansion of the deinked pulp mill at the Sheldon, Texas newsprint mill, put in operation last year, performed better than expected and allowed for production of 100% deinked newsprint and lower manufacturing costs. As a consequence, the existing thermomechanical pulp mill is no longer required and was shut-down. The Company wrote off the net book value of this pulp mill in the second quarter for a negative impact on net earnings of \$21 million or \$0.05 per share. Non-recurring items offsetting this write-off were a net gain on asset disposal of \$6 million and a change in effective tax rate on future income taxes for a non-recurring impact of \$13 million in the second quarter.

## Dividends

On June 13, 2001, the Board of Directors of the Company declared a dividend of \$0.10 per share

payable on July 3, 2001 to shareholders of record as at June 27, 2001.

## Overview of Results

A comparison of the Company's results for the six-month period ended June 30, 2001 with the corresponding period of 2000 shows significant changes in all elements. Certain indicators of pro-forma financial results are provided to assist the reader in understanding these statements. They assume that the Donohue acquisition and related debt issue took place at the beginning of each reported period.

## Selected Information

(in millions of dollars, except per share amounts)

	Three months ended June 30		Six months ended June 30	
	Actual 2001	Pro-forma 2000	Actual 2001	Pro-forma 2000
	\$	\$	\$	\$
Net Sales	1,547	1,659	3,267	3,264
Operating profit	276	227	636	419
Interest Expense	111	120	237	238
Net earnings	108	58	240	96
Earnings per share	0.25	0.13	0.55	0.22

Net sales for the second quarter of 2001 amounted to \$1.55 billion compared to pro-forma net sales of \$1.66 billion for the corresponding quarter of 2000. Operating profit was \$276 million or 17.8% of net sales for the second quarter of 2001 compared to pro-forma operating profit of \$227 million or 13.7% of pro-forma net sales for the same period of 2000.

Operating profit per business segment was as follows:

	Three months ended June 30		Six months ended June 30	
	Actual 2001	Pro-forma 2000	Actual 2001	Pro-forma 2000
	\$	\$	\$	\$
Newsprint	163	134	425	217
Value-Added Groundwood Papers and Market Pulp	89	86	203	166
Lumber	24	7	8	36

The improvement in operating profit in the second quarter of 2001 over the pro-forma operating profit of the corresponding quarter of 2000 resulted from higher selling prices for newsprint and value-added groundwood papers and lumber, partially offset by lower selling prices for pulp, downtime taken to reduce the Company's paper inventory level and write-down of Sheldon thermomechanical pulp mill of \$33 million before taxes. Synergy cost savings from the Donohue acquisition reached an annualized run rate of \$219 million in the second quarter of 2001, in line with the objective to achieve an annualized run rate of \$250 million by the end of 2001.

## **NEWSPRINT, VALUE-ADDED GROUNDWOOD PAPERS AND MARKET PULP, AND LUMBER**

### **Newsprint**

The North American newsprint market was impacted by the almost flat economic growth in the first half of 2001, lower advertising expenditures and conservation measures taken by newsprint publishers. Newsprint consumption, as reported by North American Newsprint Association was down 12.6% in the first half of 2001 when compared to the same period in 2000. Total mills and customer newsprint inventories fell by 44,000 metric tonnes during the quarter, and remain generally in line with the ten-year average.

Shipments of newsprint by the Company in the second quarter of 2001 were 314,000 metric tonnes lower than the pro-forma figure in the second quarter of 2000. This decrease is due to the permanent reduction in the Company's newsprint capacity as well as 191,000 metric tonnes of downtime taken to reduce inventory.

During the second quarter, the Company completed its program to eliminate 400,000 tonnes of high-cost newsprint capacity through the shutdown of one machine permanently and the conversion of another machine to value-added paper grades at its Kenora, Ontario mill. In addition, the Company idled the mill until the markets recover.

Due to the weak market conditions in North America during the first half of 2001, the US\$50 per tonne price increase put in place on March 1, 2001 was reduced by US\$25 on May 1, 2001. The remaining US\$25 was also withdrawn on July 1, 2001. Newsprint prices in international markets, with the exception of European countries, have also declined during the quarter.

The Company does not expect a significant recovery in demand before the fourth quarter of 2001 and also announced market-related downtime totaling approximately 150,000 tonnes to be taken in the third quarter to balance production with orders.

Permanent shutdowns and capacity conversions taking place in North America, combined with the absence of significant new capacity additions worldwide, should allow the newsprint industry to benefit when general economic conditions improve.

### **Value-Added Groundwood Papers and Market Pulp**

Demand for printing and writing paper grades has also been affected by the US economy and by lower advertising spending. According to the Pulp and Paper Products Council, consumption of uncoated groundwood papers in North America was down by 6.3% in the first half of 2001 compared to the same period in 2000.

Shipments of value-added paper grades by the Company totaled 401,000 metric tonnes in the second quarter of 2001, compared to 439,000 tonnes in the corresponding period of 2000 on a pro-forma basis. The reduction was partially attributable to the sale of its Wayagamack, Québec mill on May 8, 2001 and to 33,000 metric tonnes of maintenance and market-related downtime to control inventory levels.

Demand for Alternative Offset™ and Equal Offset™ grades was very good during the quarter. The machine in Beaupré, Québec mill is now running 100% Equal Offset™. The Company believes that the demand for glossy paper grades will continue to be weak until general economic conditions improve. Pricing for the super calendered (SC) paper grades will come under

pressure due to capacity additions and competition from lightweight coated grades in the second half of the year.

The construction of the new SC paper machine at the Lufkin, Texas mill progressed well during the quarter. The machine is in final stage of commissioning and should produce its first tonnes of paper during the summer months.

Global demand for Northern Bleached Softwood Kraft pulp (NBSK) continued to weaken during the quarter and Norscan inventories stand at 1.78 million tonnes with low operating rates of the industry during the quarter. Prices continued to erode during the quarter and no improvement in demand is expected in the short term. Following the sale of the Wayagamack mill, the Company will redirect from its other pulp mills approximately 30,000 metric tonnes of pulp previously sold to the open market to serve its internal needs.

## **Lumber**

The trade dispute between Canada and the US in respect of softwood lumber exports continues as the US Trade Commission pursued investigations under anti-dumping legislation and on the countervailing duties front. As one of the most important lumber producers in Canada, the Company has provided information in response to questionnaires from the US Trade Commission relating to the anti-dumping case. At this time, the Company cannot predict the outcome on this matter.

Sales volume in the second quarter of 2001 totaled 482 million foot board measure (MBf) compared to pro-forma sales volume of 523 MBf for the same period in 2000. Lumber prices experienced a significant surge in May but fell in June, reflecting uncertainty in the market caused by the trade dispute. Average mill nets for the quarter were 6% higher than in the same quarter in 2000.

The number of housing starts in the US remains at a high level due to low mortgage rates. The Company believes that the lumber market will remain unstable until the trade dispute is resolved and the prospect for an economic recovery is more certain.

## **Other Significant Events**

During the quarter, the Company entered into an agreement, along with Norske Skog of Norway, to jointly buy the one-third share of Pan Asia Paper Company owned by Hansol of South Korea, for a total of US\$350 million. The Company's share totaling US\$175 million will be financed by existing bank loan facilities and will raise the Company's share in the joint venture from 33% to 50%. Closing of the transaction, pending regulatory approvals in various jurisdictions, is expected at the end of the third quarter.

The Company is pursuing efforts to sell the Port-Alfred, Québec newsprint mill in accordance with its agreement with the Canadian Competition Bureau. The sale of the Wayagamack mill was completed in the second quarter for an amount of \$58 million plus working capital.

## **Financial Position and Liquidity**

Cash generated by operating activities totaled \$409 million, or \$0.93 per share for the second quarter ended June 30, 2001 compared to \$219 million or \$0.54 per share in the corresponding period in 2000. For the six-month period ended June 30, 2001, cash generated by operating activities amounted to \$551 million or \$1.25 per share compared to \$290 million or \$0.89 per share for the same period in 2000.

Capital expenditures were \$128 million in the second quarter and \$249 million for the six-month period ended June 30, 2001, including \$128 million for the Lufkin mill modernization program. The Company maintains its objective to keep its capital expenditure program below \$300 million in 2001, excluding the Texas modernization program, which will be completed this year, and its share in Pan Asia joint venture.

During the second quarter, the Company had net repayments of \$280 million of its long-term debt. As at June 30, 2001, long-term debt amounted to \$5.3 billion for a ratio of net debt to total capitalization of 0.62, compared to long-term debt of \$5.6 billion (a long-term debt ratio of 0.63 on December 31, 2000). The Company intends to apply free cash flow to the reduction of long-term debt.

**Consolidated Statement of Earnings**

(Unaudited) (in millions of Canadian dollars, except per share amounts)	Three months ended June 30		Six months ended June 30	
	2001 \$	2000 \$	2001 \$	2000 \$
Net sales	1,547	1,481	3,267	2,137
Cost of products sold	1,046	1,083	2,209	1,556
Selling, general and administrative expenses	41	46	84	62
Depreciation and amortization (note 2)	184	137	338	199
Operating profit	276	215	636	320
Interest on long-term debt	111	105	237	130
Other expenses (income)	–	(2)	9	(1)
Earnings before the following items	165	112	390	191
Income tax expense (note 3)	41	39	116	64
Non-controlling interests	6	3	14	5
Earnings before goodwill amortization	118	70	260	122
Goodwill amortization	10	9	20	10
Net earnings for the period	108	61	240	112
Earnings per share (note 4)				
Before goodwill amortization	0.27	0.17	0.59	0.37
Net earnings	0.25	0.15	0.55	0.34
Weighted average number of common shares outstanding (in millions)	440	404	440	327
Common shares outstanding at end of period (in millions)	440	440	440	440

**Consolidated Statement of Retained Earnings (Deficit)**

(Unaudited) (in millions of Canadian dollars)	Three months ended June 30		Six months ended June 30	
	2001 \$	2000 \$	2001 \$	2000 \$
Retained earnings (deficit), beginning of period	(311)	1,089	(399)	1,053
Net earnings for the period	108	61	240	112
Redemption of stock options	–	(49)	–	(49)
Acquisition dividend	–	(1,622)	–	(1,622)
Dividends declared	(44)	(44)	(88)	(59)
Deficit, end of period	(247)	(565)	(247)	(565)

## Consolidated Statement of Cash Flows

(Unaudited) (in millions of Canadian dollars, except per share amounts)	Three months ended June 30		Six months ended June 30	
	2001 \$	2000 \$	2001 \$	2000 \$
<b>Operating activities</b>				
Net earnings	108	61	240	112
Depreciation and amortization	194	146	358	209
Future income taxes	17	18	69	13
Non-controlling interests	6	3	14	5
Other non-cash items	(19)	(15)	(17)	(13)
	306	213	664	326
Change in non-cash operating working capital components (*)	103	6	(113)	(36)
Cash flows from operating activities	409	219	551	290
<b>Financing activities</b>				
Increase in long-term debt	49	2,073	185	2,161
Repayment of long-term debt	(329)	(415)	(511)	(441)
Financing fees	-	(22)	-	(22)
Acquisition dividend	-	(1,622)	-	(1,622)
Dividends paid to shareholders	(44)	-	(88)	(15)
Dividends to non-controlling shareholders of subsidiary company	(6)	(4)	(12)	(8)
Redemption of stock options	-	(49)	-	(49)
Net proceeds on issuance of shares	-	1	-	3
Cash flows from financing activities	(330)	(38)	(426)	7
<b>Investing activities</b>				
Business acquisition, net of cash acquired	-	(4)	-	(4)
Additions to capital assets	(128)	(118)	(249)	(207)
Net proceeds of disposal of capital assets	48	-	48	-
Other	-	(1)	(11)	3
Cash flows from investing activities	(80)	(123)	(212)	(208)
Increase (decrease) in cash during the period	(1)	58	(87)	89
Currency translation adjustment on cash	(1)	-	(1)	-
Cash and cash equivalents, beginning of period	37	55	123	24
Cash and cash equivalents, end of period	35	113	35	113
Cash flows from operating activities per share	0.93	0.54	1.25	0.89
(*) Components of the changes in non-cash operating working capital				
Accounts receivable	113	15	81	(1)
Inventories	43	65	(43)	16
Prepaid expenses	(5)	(3)	(26)	(8)
Accounts payable and accrued liabilities	(48)	(71)	(125)	(43)
	103	6	(113)	(36)
Cash outflows during the period related to				
Interest on long-term debt	79	94	234	115
Income taxes	14	73	9	87
	93	167	243	202

**Consolidated Balance Sheet**

(Unaudited) (in millions of Canadian dollars)	June 30, 2001 \$	December 31, 2000 \$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and short-term investments	35	123
Accounts receivable	597	681
Inventories	846	804
Prepaid expenses	77	51
	<b>1,555</b>	<b>1,659</b>
Capital assets (note 2)	7,846	8,022
Other assets	290	237
Goodwill	1,314	1,337
	<b>11,005</b>	<b>11,255</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	1,210	1,371
Long-term debt due within one year	164	327
	<b>1,374</b>	<b>1,698</b>
Long-term debt	5,165	5,265
Employee future benefits	224	262
Future income taxes (note 3)	949	875
Non-controlling interests	61	60
<b>SHAREHOLDERS' EQUITY</b>		
Capital stock	3,520	3,520
Contributed surplus	14	14
Deficit	(247)	(399)
Foreign currency translation adjustment	(55)	(40)
	<b>3,232</b>	<b>3,095</b>
	<b>11,005</b>	<b>11,255</b>

## Consolidated Business Segments

(Unaudited)

(in millions of Canadian dollars)

	Net sales \$	Depreciation and amortization \$	Operating profit \$	Addition to capital assets \$	Volume sales
<b>Three months ended June 30, 2001</b>					
Newsprint	900	131	163	44	1,088 (a)
Value-added groudwood papers and market pulp	462	41	89	76	496 (a)
Lumber	185	12	24	8	482 (b)
	<b>1,547</b>	<b>184</b>	<b>276</b>	<b>128</b>	

	Net sales \$	Depreciation and amortization \$	Operating profit \$	Addition to capital assets \$	Volume sales
<b>Three months ended June 30, 2000</b>					
Newsprint	894	90	129	25	1,257 (a)
Value-added groudwood papers and market pulp	408	35	79	84	463 (a)
Lumber	179	12	7	9	502 (b)
	<b>1,481</b>	<b>137</b>	<b>215</b>	<b>118</b>	

	Net sales \$	Depreciation and amortization \$	Operating profit \$	Addition to capital assets \$	Volume sales
<b>Six months ended June 30, 2001</b>					
Newsprint	1,958	233	425	70	2,359 (a)
Value-added groudwood papers and market pulp	991	79	203	166	1,041 (a)
Lumber	318	26	8	13	915 (b)
	<b>3,267</b>	<b>338</b>	<b>636</b>	<b>249</b>	

	Net sales \$	Depreciation and amortization \$	Operating profit \$	Addition to capital assets \$	Volume sales
<b>Six months ended June 30, 2000</b>					
Newsprint	1,275	134	177	60	1,850 (a)
Value-added groudwood papers and market pulp	519	39	114	132	604 (a)
Lumber	343	26	29	15	913 (b)
	<b>2,137</b>	<b>199</b>	<b>320</b>	<b>207</b>	

(a) in thousands of tonnes

(b) in millions of board feet

## Consolidated Business Segments (continued)

(Unaudited)  
(in millions of Canadian dollars)

	June 30, 2001	December 31, 2000
<b>Total assets</b>	<b>\$</b>	<b>\$</b>
Newsprint	7,194	7,276
Value-added groundwood papers and market pulp	3,056	3,120
Lumber	755	859
	<b>11,005</b>	<b>11,255</b>

## Notes to Consolidated Financial Statements

June 30, 2001

### 1. Summary of significant accounting policies

These financial statements are expressed in Canadian dollars and are prepared in accordance with Canadian generally accepted accounting principles.

These financial statements are prepared using the same accounting principles and application thereof as the financial statements for the year ended December 31, 2000.

#### Principles of consolidation

Effective April 18, 2000, the Company acquired the outstanding common shares of Donohue Inc. The business combination of the Company and Donohue Inc. has been accounted for using the reverse take-over method purchasing accounting.

The results of operations of Abitibi-Consolidated Inc. are included in the consolidated financial statements from April 18, 2000, the date of the business combination. Prior to that date, the results of operations of Donohue Inc. only are included in the statements.

### 2. Capital assets

During the second quarter, the Company recorded a write down of \$30 million relating to the existing thermomechanical pulp mill at its Sheldon, Texas mill. The related expense is included in depreciation in the Consolidated Statement of Earnings.

### 3. Income taxes

Due to the enactment of a reduction in a statutory tax rate and impact of corporate integration on average tax rate, the future income taxes were reduced by \$13 million in the second quarter of 2001.

### 4. Earnings per share

The exercise of stock option would have a non-dilutive effect on the earnings per share.

### 5. Subsequent event

During the quarter, the Company entered into an agreement, along with Norske Skog of Norway, to jointly buy the one-third share of Pan Asia Paper Company owned by Hansol of South Korea, for a total of US\$350 million. The Company's share totaling US\$175 million will be financed by existing bank loan facilities and will raise the Company's share in the joint venture from 33% to 50%. Closing of the transaction, pending upon regulatory approvals in various jurisdictions, is expected for the end of the third quarter of 2001.





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