

## MANAGEMENT'S DISCUSSION & ANALYSIS

### Three-month period ended March 31, 2021 compared with the three-month period ended March 31, 2020

The following is Stella-Jones Inc.'s management discussion and analysis ("MD&A"). Throughout this MD&A, the terms "Company" and "Stella-Jones" shall mean Stella-Jones Inc. with its subsidiaries, either individually or collectively.

This MD&A and the Company's condensed interim unaudited consolidated financial statements were reviewed by the Audit Committee and approved by the Board of Directors on May 2, 2021. The MD&A provides a review of the significant developments, results of operations, financial position and cash flows of the Company during the three-month period ended March 31, 2021 compared with the three-month period ended March 31, 2020. The MD&A should be read in conjunction with the Company's condensed interim unaudited consolidated financial statements for the periods ended March 31, 2021 and 2020 and the notes thereto, as well as the Company's annual audited consolidated financial statements and MD&A for the year ended December 31, 2020.

This MD&A contains statements that are forward-looking in nature. Forward-looking statements include, without limitation, the financial guidance and other statements contained in the "Updated Outlook" section below, which are provided for the purpose of assisting the reader in understanding the Company's results of operations, financial position and cash flows and management's current expectations and plans (and may not be appropriate for other purposes). Such statements are based upon a number of assumptions and involve known and unknown risks and uncertainties that may cause the actual results of the Company to be materially different from those expressed or implied by such forward-looking statements. Such items include, among others: general economic and business conditions (including the impact of the coronavirus [COVID-19] pandemic), evolution in customer demand for the Company's products and services, product selling prices, availability and cost of raw materials, changes in foreign currency rates, the ability of the Company to raise capital and factors and assumptions referenced herein and in the Company's continuous disclosure filings. Unless required to do so under applicable securities legislation, the Company's management does not assume any obligation to update or revise forward-looking statements to reflect new information, future events or other changes after the date hereof.

The Company's condensed interim unaudited consolidated financial statements are reported in Canadian dollars and are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS") and Chartered Professional Accountants ("CPA Canada") Handbook Accounting - Part I, applicable to the preparation of interim financial statements, including IAS 34, *Interim Financials Reporting*. All amounts in this MD&A are in Canadian dollars unless otherwise indicated.

This MD&A also contains financial measures which are not prescribed by IFRS and are not likely to be comparable to similar measures presented by other issuers. These measures are as follows:

- **Gross profit:** Sales less cost of sales
- **Gross profit margin:** Gross profit divided by sales for the corresponding period
- **EBITDA:** Operating income before depreciation of property, plant and equipment, depreciation of right-of-use assets and amortization of intangible assets (also referred to as earnings before interest, taxes, depreciation and amortization)
- **EBITDA margin:** EBITDA divided by sales for the corresponding period
- **Operating income margin:** Operating income divided by sales for the corresponding period
- **Cash flow from operating activities before changes in non-cash working capital components and interest and income taxes paid**
- **Net debt:** Sum of long-term debt and lease liabilities (including the current portion), short-term debt less cash and cash equivalents
- **Net debt-to-EBITDA:** Net debt divided by the trailing 12-month EBITDA

Management considers these non-IFRS measures to be useful information to assist knowledgeable investors to understand the Company's operating results, financial position and cash flows as they provide additional measures about its performance.

Additional information, including the Company's Annual Information Form, quarterly and annual reports, and supplementary information is available on the SEDAR web site at [www.sedar.com](http://www.sedar.com). Press releases and other information are also available in the Investor Relations section of the Company's web site at [www.stella-jones.com](http://www.stella-jones.com).

## OUR BUSINESS

Stella-Jones Inc. is a leading producer and marketer of pressure-treated wood products. The Company supplies North America's electrical utilities and telecommunication companies with utility poles and the continent's railroad operators with railway ties and timbers. Stella-Jones also manufactures and distributes residential lumber and accessories to retailers for outdoor applications, as well as industrial products which include wood for railway bridges and crossings, marine and foundation pilings, construction timbers, laminated poles and coal tar-based products. The Company's common shares are listed on the Toronto Stock Exchange (TSX: SJ).

As at March 31, 2021, the Company operated forty wood treating plants, twelve pole peeling facilities and a coal tar distillery. These facilities are located in six Canadian provinces and nineteen American states and are complemented by an extensive distribution network across North America. As at March 31, 2021, the Company's workforce numbered approximately 2,260 employees.

Stella-Jones possesses numerous key attributes and competitive strengths which should continue to enhance the Company's strategic positioning in the wood treating industry and enable it to generate maximum value for the Company and its stakeholders:

### *Resilient business model*

- Portfolio of businesses with steady demand
- Leadership position in product categories served
- Decentralized organisational structure with the capability to rapidly adjust to changing environments and meet urgent customer requirements
- Extensive network to service customers from multiple plants across North America
- Solid and sustained customer relationships
- Long-standing stable sources of wood supply and a registration to produce the wood preservative, creosote
- Established track record of delivering solid results

### *Seasoned management team*

- Extensive industry expertise in all divisions throughout North America
- Consistent record of successful acquisition integration and synergy capture
- Entrenched culture of entrepreneurship balanced with a focus on environmentally sound and sustainable practices

### *Solid financial position*

- Strong cash flow generation and low levels of debt
- Financial capacity to stockpile and air-season green wood for major contracts
- Financial strength and flexibility to support growth opportunities.

## **OUR MISSION**

Stella-Jones' objective is to be the performance leader in the wood preserving industry and a model corporate citizen, exercising environmental and social responsibility and integrity.

Stella-Jones will achieve these goals by focusing on customer satisfaction, core products, key markets, innovative work practices and the optimal use of its resources.

Stella-Jones is committed to providing a safe, respectful, inclusive and productive environment for its employees, where problem solving, initiative and high standards of performance are rewarded.

## **OUR STRATEGY**

Stella-Jones' strategic vision is focused on enhancing the Company's presence in its core product categories, through network efficiencies, innovation and accretive acquisitions, while seeking other strategic opportunities that leverage the Company's footprint, customer base, fibre sourcing and other competitive strengths. As one of the leading providers of industrial treated wood products, Stella-Jones generates consistent value for shareholders, and recognizes the need to integrate environmental, social and governance considerations in key decisions and strategies to enhance its business resilience and contribute to long-term value creation.

### **Capital Management**

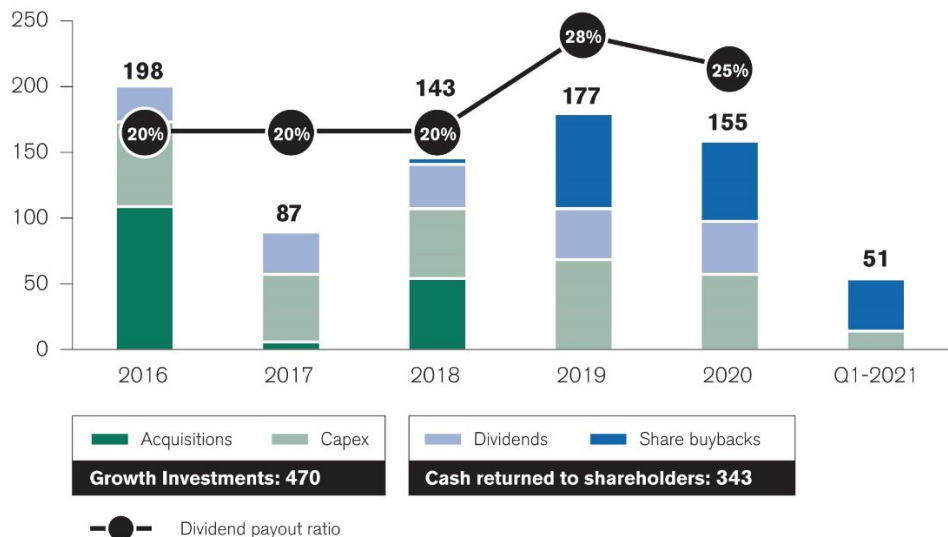
The Company's capital allocation strategy leverages its consistent and strong cash flow generation while enhancing its long-term stability and shareholder value creation. To maintain the Company's strong financial position and financial flexibility, capital is deployed in a disciplined manner, balancing growth investments and the return of capital to shareholders. The Company will:

- Invest in capital expenditures in the range of \$50 to \$60 million annually, to maintain the quality of its assets, the safety of employees and the environment, as well as support organic growth, innovation and productivity;
- Pursue accretive acquisitions that enhance the Company's strategic positioning and drive future earnings growth;
- Maintain a durable dividend payout, targeting dividends equivalent to 20% to 30% of the prior year's reported earnings per share; and
- Return excess free cash flow to shareholders through share repurchases.

As part of its capital allocation approach, Stella-Jones targets a net debt-to-EBITDA ratio between 2.0x and 2.5x. but may deviate from its leverage target to pursue acquisitions and other strategic opportunities, and/or fund its seasonal working capital requirements.

The Company's capital allocation since 2016 is summarized below:

(in millions of \$, except %)



## COVID-19 PANDEMIC

Critical to the integrity of the supply chain for utility, railroad and the construction industries, all of Stella-Jones' North American facilities have remained operational during the COVID-19 pandemic. The Company continues to reinforce measures to mitigate health risks to its employees, business partners and communities where it operates and to prevent disruptions. These measures include rigorous hygiene and cleaning practices, physical distancing policies, health monitoring and testing protocols, business travel restrictions as well as remote working. To date, the Company has not experienced a material disruption to operations, and it has not incurred significant increases in costs as a result of COVID-19. While the Company's first quarter 2021 results were strong, the impact of the ongoing COVID-19 pandemic on the demand for the Company's products, as well as on the Company's operations and those of its suppliers and customers remains uncertain and cannot currently be predicted. The duration and scope of the COVID-19 pandemic and the varying actions taken by government authorities and other businesses to reduce the spread could directly or indirectly disrupt the Company's operations and/or those of its suppliers or customers, which in turn, could adversely impact the business, financial position, results of operations and cash flows of the Company. Please refer to the Updated Outlook section for further details.

## HIGHLIGHTS

### Overview – First Quarter of 2021

Sales in the first quarter of 2021 were up 23% to \$623 million, compared to \$508 million in the first quarter last year. Pressure-treated wood sales rose by \$79 million and sales of logs and lumber increased by \$36 million. The increase in pressure-treated wood sales was primarily driven by the combination of record level market prices of lumber and the continued robust demand for residential lumber products. The upward momentum in the market price of lumber also explains the increase in sales of the logs and lumber product category.

Driven by the strong sales growth, EBITDA increased by 57% to reach \$99 million, or a margin of 15.9%, up from \$63 million, or a margin of 12.4% in the corresponding period last year. Operating income rose by 82% to \$82 million, while net income doubled to \$56 million, compared to the first quarter last year.

During the period ended March 31, 2021, Stella-Jones used its liquidity to support higher working capital requirements, invest in its property, plant and equipment and repurchase shares. As at March 31, 2021, the Company maintained a solid financial position with a net debt-to-EBITDA ratio of 2.2x.

## Financial Highlights – First Quarter of 2021

Certain prior period figures were adjusted to recognize customer freight revenues on a gross basis when the Company is the principal with respect to freight services. This change in classification from cost of sales to sales did not affect previously reported operating income and net income in the consolidated statements of income. Please refer to Note 10 in the condensed interim consolidated financial statements for the three-month periods ended March 31, 2021 and 2020.

<b>Selected Key Indicators</b> (in millions of dollars except margins and earnings per share (“EPS”))	<b>Q1-21</b>	<b>Q1-20</b>	<b>Variation (\$)</b>	<b>Variation (%)</b>
<b>Operating results</b>				
Sales <sup>(1)</sup>	623	508	115	23%
Gross profit <sup>(2)</sup>	112	83	29	35%
EBITDA <sup>(2)</sup>	99	63	36	57%
EBITDA margin <sup>(2)</sup>	15.9%	12.4%	n/a	350 bps
Operating income	82	45	37	82%
Net income	56	28	28	100%
EPS – basic & diluted	0.85	0.41	0.44	107%
<b>Cash Flows from (used in)</b>				
Operating activities	(141)	(93)	(48)	
Financing activities	155	99	56	
Investing activities	(14)	(6)	(8)	
<b>Financial position</b>	<b>As at March 31, 2021</b>	<b>As at December 31, 2020</b>	<b>Variation (\$)</b>	
Inventories	1,166	1,075	91	
Short-term debt	137	-	137	
Long-term debt <sup>(3)</sup>	663	606	57	
Lease liabilities <sup>(3)</sup>	135	139	(4)	

<sup>(1)</sup> Comparative figures have been adjusted to conform to the current period presentation.

<sup>(2)</sup> This is a non-IFRS financial measure which does not have a standardized meaning prescribed by IFRS and may therefore not be comparable to similar measures presented by other issuers.

<sup>(3)</sup> Including current portion.

## RECONCILIATION OF NON-IFRS FINANCIAL MEASURES

The following table presents the reconciliations of non-IFRS financial measures to their most comparable IFRS measures.

Reconciliation of net income to operating income and EBITDA (in millions of dollars)	Three-month period ended March 31,	
	2021	2020
Net income for the period	56	28
Plus:		
Provision for income taxes	20	10
Financial expenses	6	7
Operating income	82	45
Depreciation and amortization	17	18
EBITDA	99	63

## FOREIGN EXCHANGE

The table below shows average and closing exchange rates applicable to Stella-Jones' quarters for the years 2021 and 2020. Average rates are used to translate sales and expenses for the periods mentioned, while closing rates translate assets and liabilities of foreign operations and monetary assets and liabilities of the Canadian operations denominated in U.S. dollars.

US\$/Cdn\$ rate	2021		2020	
	Average	Closing	Average	Closing
First Quarter	1.27	1.26	1.34	1.42
Second Quarter			1.39	1.36
Third Quarter			1.33	1.33
Fourth Quarter			1.30	1.27
Fiscal Year			1.34	1.27

- Average rate: The depreciation of the value of the U.S. dollar relative to the Canadian dollar during the first quarter of 2021 compared to the first quarter of 2020 resulted in a negative impact on sales and a favourable impact on cost of sales.
- Closing rate: The depreciation of the value of the U.S. dollar relative to the Canadian dollar as at March 31, 2021, compared to December 31, 2020 resulted in a lower value of assets and liabilities denominated in U.S. dollars, when expressed in Canadian dollars.

## OPERATING RESULTS

### Sales

Sales for the first quarter reached \$623 million, up \$115 million, versus sales of \$508 million for the corresponding period last year. Excluding the negative impact of the currency conversion of \$23 million, pressure-treated wood sales rose \$102 million, or 21%, driven by pricing and volume gains in the residential lumber product category, and improved pricing for utility poles, offset in part by a reduction in sales price for railway ties, particularly for the non-Class 1 business, as detailed below. The increase in logs and lumber sales stems from the significant rise in the market price of lumber.

Sales (in millions of dollars, except percentages)	Utility Poles	Railway Ties	Residential Lumber	Industrial Products	Total Pressure- Treated Wood	Logs & Lumber	Consolidated Sales
<b>2020<sup>(1)</sup></b>	<b>207</b>	<b>172</b>	<b>71</b>	<b>29</b>	<b>479</b>	<b>29</b>	<b>508</b>
FX impact	(10)	(8)	(4)	(1)	(23)	-	(23)
Organic growth	9	(6)	99	-	102	36	138
<b>2021</b>	<b>206</b>	<b>158</b>	<b>166</b>	<b>28</b>	<b>558</b>	<b>65</b>	<b>623</b>
<b>Organic growth %</b>	<b>4%</b>	<b>(3%)</b>	<b>139%</b>	<b>-%</b>	<b>21%</b>	<b>124%</b>	<b>27%</b>

<sup>(1)</sup> Comparative figures have been adjusted to conform to the current period presentation.

### Utility Poles

Utility poles sales were \$206 million in the first quarter of 2021, in line with the corresponding period last year. Excluding the negative currency conversion effect, utility poles sales increased by nine million dollars, or 4%, driven by higher pricing, mainly in response to raw material cost increases and due to a favourable sales mix, including the impact of greater fire-resistant wrapped poles sales volume. More project-related volume this quarter was offset by lower maintenance demand, particularly in the U.S. Southeast due to extreme winter weather conditions. Utility poles sales accounted for 33% of the Company's first-quarter sales.

### Railway Ties

Railway ties sales were \$158 million in the first quarter of 2021, down 8% compared to sales of \$172 million in the same period last year. Excluding the negative currency conversion effect, railway ties sales decreased by six million dollars, or 3%, largely due to lower pricing which more than offset the increase in volumes. The reduction in sales price is attributable to continued pricing pressures and an unfavourable product mix for the non-Class 1 business, as well as downward pricing adjustments in response to lower fibre costs for Class 1 customers. While volumes were lower this quarter for Class 1 customers due to the timing of shipments, overall volumes increased as a result of the robust demand from non-Class 1 customers. Railway ties sales accounted for 25% of the Company's first-quarter sales.

### Residential Lumber

Sales in the residential lumber category rose to \$166 million in the first quarter of 2021, up 134% from sales of \$71 million in the corresponding period last year. Excluding the negative currency conversion effect, residential lumber sales increased \$99 million, or 139%. The significant increase in sales was in large part driven by the higher market price of lumber. Continued strong demand, an earlier start of the season for home improvement projects, as well as the increase in market reach as the Company gained a greater proportion of customers' annual programs, further contributed to the exceptional sales growth this quarter. As a result, residential lumber sales accounted for 27% of the Company's first-quarter sales.

### Industrial Products

Industrial product sales were \$28 million in the first quarter of 2021, relatively unchanged compared to sales of \$29 million in the first quarter last year. Lower bridge sales, mainly timing-related, were offset in large part by increased demand for pilings. Industrial product sales represented 5% of the Company's first-quarter sales.

### **Logs and Lumber**

Sales in the logs and lumber product category were \$65 million in the first quarter of 2021, more than double the sales of \$29 million generated in the corresponding period in 2020. In the course of procuring residential lumber volume, excess lumber is obtained and resold. The increase in sales this quarter is largely attributable to the significant rise in the market price of lumber. Logs and lumber sales represented 10% of the Company's first-quarter sales.

### **Sales by Geographic Region**

Sales in the United States amounted to \$404 million, or 65% of sales in the first quarter of 2021, representing an increase of \$15 million, or 4%, compared to sales of \$389 million in the first quarter of 2020. The increase is primarily due to higher pricing and demand for residential lumber, improved pricing for utility poles partially offset by a reduction in sales price for railway ties and the depreciation of the value of the U.S. dollar relative to the Canadian dollar during the first quarter of 2021 compared to the first quarter of 2020.

Sales in Canada amounted to \$219 million, or 35% of sales in the first quarter of 2021, an increase of \$100 million, or 84%, compared to sales of \$119 million in the first quarter of 2020. The significant increase is primarily attributable to higher residential lumber and logs and lumber sales due to the rise in the market price of lumber. Strong demand, an early start to the construction and outdoor renovation season and an increase in market reach further contributed to the residential lumber sales growth in Canada.

### **Cost of sales**

Cost of sales, including depreciation of property, plant and equipment, right-of-use assets as well as amortization of intangible assets, was \$511 million, or 82% of sales, in the first quarter of 2021. This compares to cost of sales of \$425 million, or 84% of sales, in the corresponding period last year. The increase in absolute dollars is explained by higher fibre costs and sales volumes for residential lumber, as well as the higher market cost of lumber for the Company's lumber trading activity, partially offset by the favourable impact of the depreciation of the U.S. dollar.

Total depreciation and amortization was \$17 million in the first quarter of 2021, with \$14 million recorded as cost of sales, compared to total depreciation and amortization of \$18 million in the corresponding period of 2020, of which \$15 million was recorded as cost of sales.

### **Gross profit**

Gross profit grew to \$112 million, or a margin of 17.9% in the first quarter of 2021, compared to \$83 million, or 16.4% of sales, in the corresponding period last year. The \$29 million increase in gross profit was primarily driven by sales price increases for residential lumber, which exceeded the higher cost of lumber, stronger residential lumber demand, as well as operational efficiency gains. Improved pricing for utility poles and volume gains for railway ties were largely offset by pricing pressures for the non-Class 1 railway ties business.

### **Selling and administrative**

Selling and administrative expenses for the first quarter of 2021 and the corresponding period in 2020 amounted to \$30 million and \$31 million respectively, including depreciation and amortization of three million for each period. Higher compensation expense, largely due to an increase in profit-sharing plan and share-based compensation accruals, was more than offset by lower project costs and reduced travel expenses.

### **Other losses, net**

Other net losses (gains) of less than one million were recorded during the first quarter of 2021, compared to seven million of other net losses recognized in the corresponding quarter of 2020. Most of the other net losses in the prior year period consisted of unrealized mark-to-market losses related to diesel derivative commodity contracts, which expired at the end of 2020.

### **Operating income**

Operating income totalled \$82 million, or 13.1% of sales, in the first quarter of 2021. In the corresponding period of 2020, operating income totalled \$45 million, or 8.8% of sales and included seven million of other net losses.



### Financial expenses

Financial expenses amounted to six million in the first quarter of 2021, down slightly compared to the seven million expense recorded in the corresponding period last year. This variation is due to a decrease in interest rates, partially offset by additional borrowings.

### Income before income taxes and income tax expense

Income before income taxes was \$76 million, or 12.1% of sales, in the first quarter of 2021, versus \$38 million, or 7.5% of sales, in the corresponding period of 2020. The provision for income taxes totalled \$20 million in the first quarter of 2021, compared to \$10 million in the same period last year, representing an effective tax rate of approximately 26%.

### Net income

Net income for the first quarter of 2021 was \$56 million, or \$0.85 per share, double the net income of \$28 million, or \$0.41 per share, in the corresponding period of 2020.

## QUARTERLY RESULTS

The Company's sales follow a seasonal pattern, with utility poles, railway ties, and industrial product shipments stronger in the second and third quarters to provide industrial end users with product for their summer maintenance projects. Residential lumber sales also follow a similar seasonal pattern. In the fall and winter seasons, there tends to be less activity; as a result, the first and fourth quarters are typically characterized by relatively lower sales. The table below sets forth selected financial information for the Company's last nine quarters, ending with the most recently completed financial year:

### 2021

For the quarters ended (in millions of dollars, except EPS)	March 31	June 30	Sept. 30	Dec. 31	Total
Sales	623				
EBITDA <sup>(2)</sup>	99				
Operating income	82				
Net income for the period	56				
EPS - basic and diluted	0.85				

### 2020

For the quarters ended (in millions of dollars, except EPS)	March 31	June 30	Sept. 30	Dec. 31	Total
Sales <sup>(1)</sup>	508	768	742	533	2,551
EBITDA <sup>(2)</sup>	63	120	132	70	385
Operating income	45	101	113	50	309
Net income for the period	28	69	79	34	210
EPS - basic and diluted	0.41	1.02	1.17	0.52	3.12

### 2019

For the quarters ended (in millions of dollars, except EPS)	March 31	June 30	Sept. 30	Dec. 31	Total
Sales <sup>(1)</sup>	446	667	631	445	2,189
EBITDA <sup>(2)</sup>	64	94	96	59	313
Operating income	46	77	78	41	242
Net income for the period	29	52	54	28	163

EPS - basic and diluted	0.43	0.76	0.77	0.41	2.37
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<sup>(1)</sup> Comparative figures have been adjusted to conform to the current period presentation.

<sup>(2)</sup> This is a non-IFRS financial measure which does not have a standardized meaning prescribed by IFRS and may therefore not be comparable to similar measures presented by other issuers.

## STATEMENT OF FINANCIAL POSITION

As a majority of the Company's assets and liabilities are denominated in U.S. dollars, exchange rate variations may significantly affect their value. As such, the depreciation of the U.S. dollar relative to the Canadian dollar as at March 31, 2021, compared to December 31, 2020 (see "Foreign Exchange" on page 6), results in a lower amount of assets and liabilities denominated in U.S. dollars, when expressed in Canadian dollars.

### Assets

As at March 31, 2021, total assets stood at \$2,675 million versus \$2,426 million as at December 31, 2020. The increase in total assets largely reflects higher current assets, as detailed below. Note that the following table provides information on assets using select line items from the consolidated statements of financial position.

Assets (in millions of dollars)	As at March 31, 2021	As at December 31, 2020	Variance
Accounts receivable	376	208	168
Inventories	1,166	1,075	91
Other current assets	34	36	(2)
<b>Total current assets</b>	<b>1,576</b>	<b>1,319</b>	<b>257</b>
Property, plant and equipment	573	574	(1)
Right-of-use assets	130	135	(5)
Intangible assets	117	115	2
Goodwill	276	280	(4)
Other non-current assets	3	3	-
<b>Total non-current assets</b>	<b>1,099</b>	<b>1,107</b>	<b>(8)</b>
<b>Total assets</b>	<b>2,675</b>	<b>2,426</b>	<b>249</b>

Accounts receivable, net of a credit loss allowance of less than one million, was \$376 million as at March 31, 2021, compared to \$208 million as at December 31, 2020. The increase was attributable to the normal seasonal demand increase near the end of the quarter and higher sales for residential lumber. In the normal course of business, the Company has entered into facilities with certain financial institutions whereby it can sell, without credit recourse, eligible trade receivables to the concerned financial institutions.

Inventories stood at \$1,166 million as at March 31, 2021, up from \$1,075 million as at December 31, 2020. The increase is explained by the seasonal inventory build-up ahead of peak demand in the second and third quarters as well as the higher cost of residential lumber inventory given the rise in the market price of lumber, partially offset by the effect of currency translation of U.S. dollar denominated inventories.

Given the long periods required to air-season wood, which can occasionally exceed nine months before a sale is concluded, inventories are a significant component of working capital and the turnover is relatively low. In addition, significant raw material and finished goods inventory are required at certain times of the year to support the residential lumber product category. The Company maintains solid relationships and enters into long-term contracts with customers to better ascertain inventory requirements. Management continuously monitors the levels of inventory and market demand for its products and production is adjusted accordingly to optimize efficiencies and capacity utilization.

Property, plant and equipment stood at \$573 million as at March 31, 2021, compared with \$574 million as at December 31, 2020. The decrease reflects depreciation expense of six million dollars and the effect of currency translation of U.S. dollar denominated property, plant and equipment, largely offset by the purchase of property, plant and equipment of \$10 million during the first quarter of 2021.

Right-of-use assets totalled \$130 million as at March 31, 2021, compared to \$135 million as at December 31, 2020. The decrease is primarily due to the depreciation expense of nine million dollars for the first quarter of 2021, partially offset by the addition of right-of-use-assets, largely rolling stock, of five million dollars.

Intangible assets and goodwill totalled \$117 million and \$276 million, respectively, as at March 31, 2021. Intangible assets consist mainly of customer relationships, a creosote registration, software costs and cutting rights. As at December 31, 2020, intangible assets and goodwill were \$115 million and \$280 million, respectively. Intangible assets increased as additions during the period associated with the implementation of a new enterprise resource planning system were partially offset by the amortization expense of two million. The decrease in goodwill is explained by the effect of currency translation on U.S.-based goodwill.

## Liabilities

As at March 31, 2021, Stella-Jones' total liabilities stood at \$1,304 million, up from \$1,053 million as at December 31, 2020. The increase in total liabilities mainly reflects the increase in current liabilities, as detailed below. Note that the following table provides information on liabilities using select line items from the consolidated statements of financial position.

<b>Liabilities</b> (in millions of dollars)	<b>As at March 31, 2021</b>	<b>As at December 31, 2020</b>	<b>Variance</b>
Short-term debt	137	-	137
Accounts payable and accrued liabilities	201	137	64
Current portion of long-term debt	74	11	63
Current portion of lease liabilities	33	33	-
Other current liabilities	42	37	5
<b>Total current liabilities</b>	<b>487</b>	<b>218</b>	<b>269</b>
Long-term debt	589	595	(6)
Lease liabilities	102	106	(4)
Other non-current liabilities	126	134	(8)
<b>Total non-current liabilities</b>	<b>817</b>	<b>835</b>	<b>(18)</b>
<b>Total liabilities</b>	<b>1,304</b>	<b>1,053</b>	<b>251</b>

Current liabilities were \$487 million as at March 31, 2021, versus \$218 million as at December 31, 2020. This variation is primarily attributable to an increase in short-term debt of \$137 million to support seasonal working capital requirements amplified this year by higher demand and the record high market price of lumber, the reclassification of the US\$50 million unsecured non-revolving term facility due in February 2022 to current portion of long-term debt, and a \$64 million increase in accounts payable and accrued liabilities, largely due to the seasonal inventory build-up in the first quarter of 2021.

During the quarter, the Company borrowed \$74 million (US\$59 million) under the demand loan facility and presented this indebtedness as short-term debt. The demand loan agreement was amended on February 15, 2021 to increase the amount available from US\$50 to US\$100 million until June 30, 2021. As at March 31, 2021, the Company had \$52 million (US\$41 million) available under the demand loan facility.

In addition, on March 12, 2021, Stella-Jones Corporation ("SJC"), a wholly-owned U.S. subsidiary of the Company, entered into a letter loan agreement with a lender within the United States farm credit system, pursuant to which a term loan of US\$100 million (the "Bridge Loan") was made available to SJC. The first installment of US\$50 million under the Bridge Loan was advanced in March 2021 and presented as short-term debt. The second US\$50 million installment was advanced in April 2021. On April 29, 2021, the Bridge Loan was repaid in full. Please refer to the Subsequent Events section for additional information.

The Company's long-term debt, including the current portion, was \$663 million as at March 31, 2021, up from \$606 million as at December 31, 2020. Additional borrowings during the quarter of \$63 million were partly offset by the currency translation effect on U.S. dollar denominated long-term debt. The Company's syndicated credit facilities of \$471 million (US\$375 million) were fully drawn at the end of the quarter.

As at March 31, 2021, the net debt-to-EBITDA ratio increased to 2.2x from 1.9x at the end of the fourth quarter of 2020 and the Company was in full compliance with its debt covenants, reporting requirements and financial ratios.

### Shareholders' equity

Shareholders' equity stood at \$1,371 million as at March 31, 2021, compared to \$1,373 million as at December 31, 2020.

Shareholders' Equity (in millions of dollars)	As at March 31, 2021	As at December 31, 2020	Variance
Capital Stock	212	214	(2)
Retained earnings	1,091	1,079	12
Accumulated other comprehensive income	68	80	(12)
<b>Total shareholders' equity</b>	<b>1,371</b>	<b>1,373</b>	<b>(2)</b>

The decrease in shareholders' equity as at March 31, 2021 is attributable to a \$12 million decrease in accumulated other comprehensive income, mainly due to the foreign operations currency translation adjustment, \$37 million of share repurchases and \$12 million of dividends declared in the quarter, partially offset by net income of \$56 million generated in the first quarter of 2021.

On August 4, 2020, the TSX accepted Stella-Jones' Notice of Intention to Make a Normal Course Issuer Bid ("NCIB"). Stella-Jones may, during the 12-month period commencing August 10, 2020 and ending August 9, 2021, purchase for cancellation, up to 2,500,000 common shares.

On March 9, 2021, the Company received approval from the TSX to amend its NCIB in order to increase the maximum number of common shares that may be repurchased for cancellation by the Company from 2,500,000 to 3,500,000 common shares. All other terms and conditions of the NCIB remained unchanged. The amendment to the NCIB was effective on March 15, 2021 and will continue until August 9, 2021 or such earlier date as Stella-Jones has acquired the maximum number of common shares permitted under the NCIB.

In the three-month period ended March 31, 2021, the Company repurchased 801,261 common shares for cancellation in consideration of \$37 million. Since the beginning of the NCIB on August 10, 2020, the Company repurchased 2,132,716 common shares for cancellation in consideration of \$97 million.

## LIQUIDITY AND CAPITAL RESOURCES

The following table sets forth summarized cash flow components for the periods indicated:

Summary of cash flows (in millions of dollars)	Three-month period ended March 31,	
	2021	2020
Operating activities	(141)	(93)
Financing activities	155	99
Investing activities	(14)	(6)
Net change in cash and cash equivalents during the period	-	-
Cash and cash equivalents - Beginning	-	-
<b>Cash and cash equivalents – End</b>	<b>-</b>	<b>-</b>

The Company believes that its cash flow from operations and available credit facilities are adequate to finance its business plans, meet its working capital requirements and maintain its assets.

### Cash flows from (used in) operating activities

Cash flows used in operating activities amounted to \$141 million in the first quarter of 2021, compared to \$93 million in the corresponding period in 2020, mainly due to an increase in non-cash working capital components, partially offset by improved profitability. Cash flows from operating activities before changes in non-cash working capital components and interest and income taxes paid was \$100 million in the first quarter of 2021, compared to \$69 million in the corresponding period in 2020. Changes in non-cash working capital components decreased liquidity by \$213 million in the first quarter of 2021, largely due to the seasonal increase in working capital, the higher level of sales and the increased inventory costs stemming from the higher market price of lumber. The following table provides information on cash flows provided by operating activities using select line items from the consolidated statements of cash flows.

Cash flows from (used in) operating activities (in millions of dollars)	Three-month period ended March 31,	
	2021	2020
Net income	56	28
Depreciation and amortization	17	18
Current income tax expense	22	11
Financial expenses	6	7
Others	(1)	5
<b>Cash flows from operating activities before changes in non-cash working capital components and interest and income taxes paid</b>	<b>100</b>	<b>69</b>
Accounts receivable	(171)	(94)
Inventories	(99)	(86)
Other current assets	2	-
Accounts payable and accrued liabilities	55	27
<b>Changes in non-cash working capital components</b>	<b>(213)</b>	<b>(153)</b>
Interest paid	(8)	(8)
Income taxes paid	(20)	(1)
<b>Cash flows from (used in) operating activities</b>	<b>(141)</b>	<b>(93)</b>

### Cash flows from (used in) financing activities

Financing activities in the first quarter of 2021 increased liquidity by \$155 million. During the quarter ended March 31, 2021, the Company increased its short-term debt by \$137 million, borrowed \$63 million under its syndicated credit facilities, repurchased common shares for \$37 million and repaid eight million dollars of lease liabilities. In the first quarter of 2020, financing activities increased liquidity by \$99 million as the Company borrowed \$108 million under its credit facilities and repaid eight million dollars of lease liabilities. The following table provides information on cash flows used in financing activities using select line items from the consolidated statements of cash flows.

Cash flows from (used in) financing activities (in millions of dollars)	Three-month period ended March 31,	
	2021	2020
Increase in short-term debt	137	-
Net change in syndicated credit facilities	63	108
Repayment of long-term debt	-	(1)
Repayment of lease liabilities	(8)	(8)
Repurchase of common shares	(37)	-
<b>Cash flows from financing activities</b>	<b>155</b>	<b>99</b>

### Cash flows used in investing activities

Investing activities used liquidity of \$14 million in the first quarter of 2021, explained by the purchase of property, plant and equipment and expenditures related to the implementation of the enterprise resource planning system. In the first quarter of 2020, investing activities totalled six million and primarily consisted of the purchase of property, plant and equipment, as detailed below. The following table provides information on cash flows used in investing activities using select line items from the consolidated statements of cash flows.

Cash flows used in investing activities (in millions of dollars)	Three-month period ended March 31,	
	2021	2020
Purchase of property, plant and equipment	(10)	(5)
Additions of intangible assets	(4)	(1)
<b>Cash flows used in investing activities</b>	<b>(14)</b>	<b>(6)</b>

### Financial obligations

The following table details the maturities of the financial obligations as at March 31, 2021:

Financial obligations (in millions of dollars)	Carrying Amount	Contractual Cash flows	Less than 1 year	Years 1-3	Years 4-5	More than 5 years
Short-term debt	137	137	137	-	-	-
Accounts payable and accrued liabilities	201	201	201	-	-	-
Long-term debt obligations <sup>(1)</sup>	663	721	88	124	410	99
Minimum payments under lease liabilities	135	148	37	53	28	30
Derivative financial instruments	1	1	1	-	-	-
Non-compete agreements	1	1	1	-	-	-
<b>Financial obligations</b>	<b>1,138</b>	<b>1,209</b>	<b>465</b>	<b>177</b>	<b>438</b>	<b>129</b>

<sup>(1)</sup> Includes interest payments. Interest on variable interest debt is assumed to remain unchanged from the rates in effect as at March 31, 2021.

## SHARE AND STOCK OPTION INFORMATION

As at March 31, 2021, the capital stock issued and outstanding of the Company consisted of 65,392,450 common shares (December 31, 2020 – 66,187,404).

The following table presents the outstanding capital stock activity for the three-month period ended March 31, 2021:

<b>Number of shares</b>	<b>Three-month period ended March 31, 2021</b>
Balance – Beginning of period	66,187,404
Common shares repurchased	(801,261)
Employee share purchase plans	6,307
<b>Balance – End of period</b>	<b>65,392,450</b>

As at April 30, 2021, the capital stock issued and outstanding consisted of 65,393,234 common shares.

As at March 31, 2021, the number of outstanding and exercisable options to acquire common shares issued under the Company’s Stock Option Plan was 30,000 (December 31, 2020 – 30,000). As at May 2, 2021, the number of outstanding and exercisable options was 30,000.

## COMMITMENTS AND CONTINGENCIES

The commitments and contingencies susceptible to affect the Company in the future remain substantially unchanged from those included in the Company’s annual MD&A contained in its 2020 Annual Report.

## SUBSEQUENT EVENTS

On April 29, 2021, SJC entered into a credit agreement (the “US Credit Agreement”) with a syndicate of lenders within the United States farm credit system, pursuant to which senior unsecured credit facilities of up to US\$350 million were made available, including a term loan facility of up to US\$250 million and a revolving credit facility of US\$100 million. The US Credit Agreement includes representations, warranties, covenants and events of default substantially similar to those under the existing syndicated credit agreement. On April 29, 2021, a drawdown of US\$100 million was made under the revolving credit facility, and the proceeds thereof were used to repay the Bridge Loan in full.

On May 2, 2021, the Board of Directors declared a quarterly dividend of \$0.18 per common share payable on June 22, 2021 to shareholders of record at the close of business on June 1, 2021. This dividend is designated to be an eligible dividend.

The declaration, amount and date of any future dividends will continue to be considered by the Board of Directors of the Company based on the Company’s capital allocation strategy. There can be no assurance as to the amount or timing of such dividends in the future.

## **RISKS AND UNCERTAINTIES**

Except as described in the COVID-19 Pandemic section herein, the risks and uncertainties affecting the Company in the future remain substantially unchanged from those included in the Company's annual MD&A contained in its 2020 Annual Report.

## **SIGNIFICANT ACCOUNTING POLICIES**

The Company's significant accounting policies are described in Note 2 to the December 31, 2020 and 2019 audited consolidated financial statements.

The Company prepares its consolidated financial statements in accordance with IFRS and CPA Canada Handbook Accounting - Part I.

The preparation of consolidated financial statements in conformity with IFRS requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Significant items subject to estimates and assumptions include estimated useful life of assets, recoverability of long-lived assets and goodwill and determination of the fair value of the assets acquired and liabilities assumed in the context of an acquisition. It is possible that actual results could differ from those estimates, and such differences could be material. Estimates are reviewed periodically and, as adjustments become necessary, they are reported in the consolidated statement of income in the period in which they become known.

## **DISCLOSURE CONTROLS AND PROCEDURES**

The Company maintains appropriate information systems, procedures and controls to ensure that information used internally and disclosed externally is complete, accurate, reliable and timely. The disclosure controls and procedures ("DC&P") are designed to provide reasonable assurance that information required to be disclosed in the annual filings, interim filings or other reports filed under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation and include controls and procedures designed to ensure that information required to be disclosed is accumulated and communicated to Management, including its certifying officers, as appropriate to allow timely decisions regarding required disclosure.

The President and Chief Executive Officer and the Senior Vice-President and Chief Financial Officer of the Company have evaluated, or caused the evaluation of, under their direct supervision, the design effectiveness of the Company's DC&P (as defined in Regulation 52-109 - Certification of Disclosure in Issuer's Annual and Interim Filings) as at March 31, 2021 and have concluded that such DC&P were designed effectively.

## **INTERNAL CONTROL OVER FINANCIAL REPORTING**

Management is responsible for establishing and maintaining adequate internal controls over financial reporting ("ICFR") to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

Management has evaluated the design effectiveness of its ICFR as defined in Regulation 52-109 – Certification of Disclosure in Issuer's Annual and Interim Filings. The evaluation was based on the criteria established in the "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). This evaluation was performed by the President and Chief Executive Officer and the Senior Vice-President and Chief Financial Officer of the Company with the assistance of other Company Management and staff to the extent deemed necessary. Based on this evaluation, the President and Chief Executive



Officer and the Senior Vice-President and Chief Financial Officer concluded that the ICFR were appropriately designed effectively, as at March 31, 2021.

In spite of its evaluation, Management does recognize that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance and not absolute assurance of achieving the desired control objectives.

## **CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING**

No changes were made to the design of ICFR during the period from January 1, 2021 to March 31, 2021 that have materially affected or are reasonably likely to materially affect the Company's ICFR.

## **UPDATED OUTLOOK**

The Company's financial outlook provided in the MD&A for the year ended December 31, 2020 is updated to reflect the strong quarterly performance, largely attributable to the unprecedented rise in the market price of lumber, and the expectation that the higher levels of pricing for lumber will continue to favourably impact the profitability of the residential lumber product category during the seasonal peak demand period.

Stella-Jones is now targeting to deliver EBITDA in the range of \$450 to \$480 million in 2021, up from the previously disclosed guidance of \$385 to \$410 million. This updated guidance anticipates a reduction of approximately \$90 million in sales from the depreciation of the value of the U.S. dollar relative to the Canadian dollar to C\$1.27 per U.S. dollar.

Excluding the impact of the currency conversion, the Company is projecting 2021 sales growth of 15% to low 20% range compared to 2020. The projected 2021 sales for utility poles, railway ties and industrial products remain unchanged. Utility poles sales are expected to increase in the mid to high-single digit range compared to 2020, due to sustained healthy replacement demand, including an increase in value-added fire-resistant wrapped pole sales, while railway ties and industrial product sales are projected to be relatively comparable to those generated in 2020. For residential lumber, sales are now forecasted to increase in the range of 45% to 65% compared to 2020, driven by the current trend of higher pricing, which is projected to continue during the seasonal peak demand period for this product category.

The Company has made a number of economic and market assumptions in preparing the guidance and making the forward-looking statements contained herein.

These assumptions include, but are not limited to the following:

- Impacts of the COVID-19 pandemic on the demand for the Company's core product categories will be largely in line with those experienced in 2020;
- No significant reduction in the maintenance programs of major railway and utility pole customers;
- No major disruption in the Company's manufacturing operations, supply chain and distribution networks, other than the measures already adopted by the Company to mitigate health risks to its employees, business partners and communities where it operates in response to COVID-19;
- Canadian dollar will trade, on average, at approximately C\$1.27 per U.S. dollar, with sales in the United States continuing to represent approximately 70% of total sales;
- Impact of potential acquisitions are not included.

This outlook is fully qualified by the forward-looking statements described in this MD&A.

May 2, 2021