MANAGEMENT'S DISCUSSION & ANALYSIS

Three-and six-month periods ended June 30, 2021 compared with the three- and six-month periods ended June 30, 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 August 2, 2021. The MD&A provides a review of the significant developments, results of operations, financial position and cashflows of the Company during the three-and six-month periods ended June 30, 2021 compared with the three-and six-month periods ended June 30, 2020. The MD&A should be read in conjunction with the Company's condensed interim unaudited consolidated financial statements for the periods ended June 30, 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 financial position, results of operations 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. Press releases and other information are also available in the Investor Relations section of the Company's web site at 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 June 30, 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 June 30, 2021, the Company's workforce numbered approximately 2,340 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 organizational 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 importance of integrating environmental, social and governance considerations into key decisions and strategies to enhance its business resilience and contribute to long-term value creation.

Capital Management

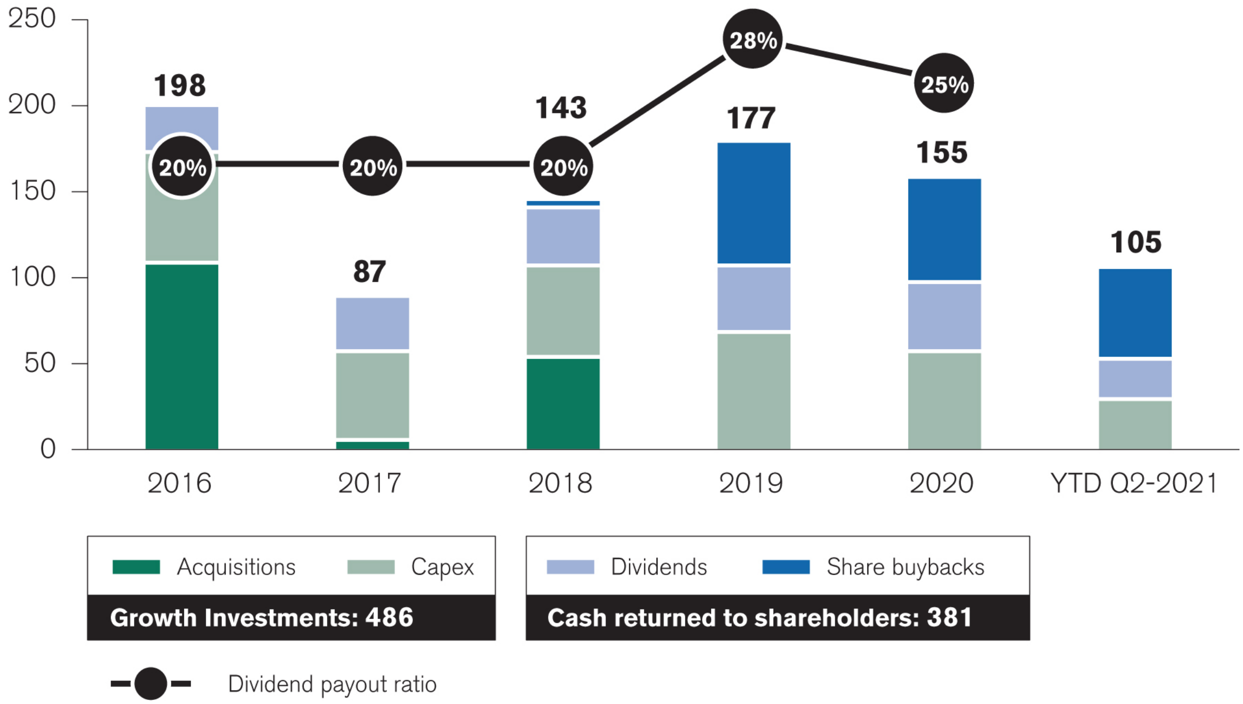
The Company's capital allocation strategy leverages its consistent and strong cash flow generation while enhancing its long-term stability and shareholder value creation. To maintain the Company's strong financial position and financial flexibility, capital is deployed in a disciplined manner, balancing 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. 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 second 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 – Second Quarter of 2021

Sales in the second quarter of 2021 were up 18% to $903 million, compared to $768 million last year, despite a $65 million negative impact from currency conversion. Excluding the impact of the currency conversion, pressure-treated wood sales rose by $136 million and sales of logs and lumber increased by $64 million. The increase in pressure-treated wood sales was driven by growth in the Company's three core product categories: residential lumber benefited from the unprecedented high market prices of lumber, utility poles benefited from increased volumes, upward price adjustments and an improved sales mix while railway ties sales growth stemmed from volume gains. The rise in market lumber prices during the quarter also explains the increase in sales of the logs and lumber product category. Driven by the strong sales growth, EBITDA increased by 50% this quarter to a new record high of $180 million, or a margin of 20%, up from $120 million, or a margin of 15.6% last year.

During the second quarter ended June 30, 2021, Stella-Jones used the cash generated from operations to invest in capital expenditures, reduce the indebtedness related to the seasonal investment in working capital in the first quarter, pay dividends and repurchase shares. As at June 30, 2021, the Company maintained a strong financial position with a net debt to trailing 12-month EBITDA ratio of 1.7x.

Financial Highlights – Second Quarter of 2021

Selected Key Indicators (in millions of dollars except margins and earnings per share ("EPS"))	**Q2-21**	**Q2-20**	**Variation ($)**	**Variation (%)**
Operating results				
Sales	903	768	135	18%
Gross profit[1]	197	131	66	50%
Gross profit margin[1]	21.8%	17.1%	n/a	470 bps
EBITDA[1]	180	120	60	50%
EBITDA margin[1]	20.0%	15.6%	n/a	440 bps
Operating income	161	101	60	59%
Net income	115	69	46	67%
EPS – basic & diluted	1.76	1.02	0.74	73%
Cash Flows from (used in)				
Operating activities	173	146	27	
Financing activities	(156)	(136)	(20)	
Investing activities	(17)	(10)	(7)	
Financial position	**As at June 30, 2021**	**As at December 31, 2020**	**Variation ($)**	
Inventories	1,120	1,075	45	
Long-term debt[2]	682	606	76	
Lease liabilities[2]	138	139	(1)	

[1] 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.

[2] Including current portion.

Financial Highlights - Year-To-Date

Selected Key Indicators (in millions of dollars except margins and EPS)	**YTD Q2-21**	**YTD Q2-20**	**Variation ($)**	**Variation (%)**
Operating results				
Sales	1,526	1,276	250	20%
Gross profit[(1)]	309	214	95	44%
Gross profit margin[(1)]	20.2%	16.8%	n/a	340 bps
EBITDA[(1)]	279	183	96	52%
EBITDA margin[(1)]	18.3%	14.4%	n/a	390 bps
Operating income	243	146	97	66%
Net income	171	97	74	76%
EPS – basic & diluted	2.61	1.43	1.18	83%
Cash Flows from (used in)				
Operating activities	32	53	(21)	
Financing activities	(1)	(37)	36	
Investing activities	(31)	(16)	(15)	

(1) 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.

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 EBITDA (in millions of dollars)	**Three-month periods ended June 30**		**Six-month periods ended June 30**	
	2021	**2020**	**2021**	**2020**
Net income for the period	115	69	171	97
Plus:				
Provision for income taxes	40	25	60	35
Financial expenses	6	7	12	14
Operating income	161	101	243	146
Depreciation and amortization	19	19	36	37
EBITDA	180	120	279	183

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	1.23	1.24	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 second quarter of 2021 compared to the second 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 June 30, 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 second quarter of 2021 reached $903 million, up $135 million, versus sales of $768 million for the corresponding period last year. Excluding the negative impact of the currency conversion of $63 million, pressure-treated wood sales rose $136 million, or 18%, primarily driven by higher pricing for residential lumber which more than offset the decrease in demand, pricing and volume gains and a better sales mix for utility poles, and an increase in railway ties volumes, as detailed below. The increase in logs and lumber sales stems from the unprecedented 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**
Q2-2020	**230**	**225**	**257**	**33**	**745**	**23**	**768**
FX impact	(24)	(24)	(11)	(4)	**(63)**	(2)	**(65)**
Organic growth	30	15	84	7	**136**	64	**200**
Q2-2021	**236**	**216**	**330**	**36**	**818**	**85**	**903**
Organic growth %	13%	7%	33%	21%	**18%**	278%	**26%**

For the first six months of 2021, sales amounted to $1.53 billion, versus $1.28 billion for the corresponding period last year. Excluding the negative impact of the currency conversion of $86 million, pressure-treated wood sales rose by $238 million, or 19%, and logs and lumber sales grew by $100 million. The year-over-year sales growth in pressure-treated wood stems from the significant rise in the market prices of lumber offset in part by a decrease in residential lumber volumes. Sales also grew due to the increased demand, upward pricing adjustments and an improved sales mix for utility poles, as well as, higher volumes for railway ties which outweighed the pricing pressures for the non-Class 1 business, as detailed below. The exceptional increase in logs and lumber sales stems from the unprecedented increase in market prices 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**
YTD 2020	**437**	**397**	**328**	**62**	**1,224**	**52**	**1,276**
FX impact	(34)	(32)	(15)	(5)	**(86)**	(2)	**(88)**
Organic growth	39	9	183	7	**238**	100	**338**
YTD 2021	**442**	**374**	**496**	**64**	**1,376**	**150**	**1,526**
Organic growth %	9%	2%	56%	11%	**19%**	192%	**26%**

Utility poles

Utility poles sales increased to $236 million in the second quarter of 2021, compared to sales of $230 million in the corresponding period last year. Excluding the currency conversion effect, utility poles sales increased by $30 million, or 13%, driven by improved maintenance demand for distribution poles, upward price adjustments and a better sales mix, including the impact of additional fire-resistant wrapped pole sales volumes. This growth was partially offset by less project-related volumes. Utility poles sales accounted for 26% of the Company's second-quarter sales.

For the first six months of 2021, utility poles sales totaled $442 million, versus $437 million for the corresponding period last year. Excluding the currency conversion effect, utility pole sales increased $39 million, or 9%, due to volume and pricing gains and a favourable sales mix.

Railway ties
Railway ties sales were $216 million in the second quarter of 2021, compared to sales of $225 million in the same period last year. Excluding the currency conversion effect, railway ties sales increased $15 million, or 7%, largely attributable to higher volumes for Class 1 customers due to the timing of shipments. The higher sales volumes were offset in part by pricing pressures for non-Class 1 customers, which eased somewhat during the quarter. Railway ties sales accounted for 24% of the Company's second-quarter sales.

For the first six months of 2021, railway ties sales totaled $374 million, versus $397 million for the corresponding period last year. Excluding the currency conversion effect, railway ties sales increased nine million, or 2%, primarily explained by higher volumes stemming from solid non-Class 1 demand and timing of Class 1 shipments, partially offset by pricing headwinds, particularly for non-Class 1 business.

Residential lumber
Sales in the residential lumber category rose to $330 million in the second quarter of 2021, compared to sales of $257 million in the corresponding period last year. Excluding the currency conversion effect, residential lumber sales increased $84 million, or 33%, driven by the exceptional rise in the market price of lumber. This increase was partially offset by lower sales volumes attributable to softening consumer demand. Residential lumber sales accounted for 37% of the Company's second-quarter sales.

For the first six months of 2021, residential lumber sales totaled $496 million versus $328 million for the corresponding period last year. Excluding the currency conversion effect, residential lumber sales were up 56%. The unprecedented market-driven pricing gains outweighed the decrease in volumes in the second quarter.

Industrial products
Industrial product sales were $36 million in the second quarter of 2021 compared to sales of $33 million in the second quarter last year, largely due to more timber and piling projects, offset in part by lower project-related bridge and crossing sales. Industrial product sales represented 4% of the Company's second-quarter sales.

For the first six months of 2021, industrial product sales totaled $64 million, compared to $62 million in the corresponding period last year. Excluding the currency conversion effect, industrial product sales increased $7 million, or 11%. The year-over-year increase was entirely generated in the second quarter.

Logs and lumber
Sales in the logs and lumber product category were $85 million in the second quarter of 2021, up over three-fold compared to $23 million in the corresponding period last year. The exceptional increase is due to the rise in the market price of lumber during the quarter. Logs and lumber sales represented 9% of the Company's second-quarter sales.

For the first six months of 2021, sales in the logs and lumber product category totaled $150 million versus $52 million for the corresponding period last year, explained by the all-time high market price of lumber during the first half of the year.

Sales by Geographic Region
Sales in the United States amounted to $503 million, or 56% of sales in the second quarter of 2021, up $11 million, or 2%, compared to sales of $492 million in the corresponding period last year. The increase is primarily due to higher pricing for residential lumber offset in part by lower volumes, improved pricing and demand for utility poles and volume gains for railway ties. The depreciation of the value of the U.S. dollar relative to the Canadian dollar during the second quarter of 2021 compared to the same period last year negatively impacted sales in 2021. For the first six months of 2021, sales in the United States stood at $908 million, up from $881 million in the corresponding period last year.

Sales in Canada amounted to $400 million, or 44% of sales in the second quarter of 2021, an increase of $124 million, or 45%, compared to sales of $276 million in the second quarter last year. The increase is mainly attributable to higher residential lumber and logs and lumber sales stemming from the increase in the market price of lumber, offset in part by lower residential lumber volumes. For the first six months of 2021, sales in Canada stood at $618 million, up from $395 million in the corresponding period last year.

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 $706 million, or 78% of sales, in the second quarter of 2021. This compares to cost of sales of $637 million, or 83% of sales, in the corresponding period last year. The increase in absolute dollars is largely explained by higher fibre costs, particularly for residential lumber and for the Company's lumber trading activity, partially offset by overall lower sales volumes and the favourable impact of the depreciation of the U.S. dollar.

Total depreciation and amortization was $19 million in the second quarter of 2021, with $16 million recorded as cost of sales, unchanged compared to the corresponding period last year.

For the first six months of 2021, cost of sales, including depreciation of property, plant and equipment, right-of-use assets as well as amortization of intangible assets, was $1,217 million, or 80% of sales. This compares to cost of sales of $1,062 million, or 83% of sales, in the corresponding period last year. Total depreciation and amortization was $36 million, with $30 million recorded as cost of sales, compared to total depreciation and amortization of $37 million in the corresponding period last year, of which $31 million was recorded as cost of sales.

Gross profit

Gross profit grew to $197 million, or 22% of sales, in the second quarter of 2021, compared to $131 million, or 17% of sales, in the corresponding period last year. The absolute dollar increase was primarily driven by the rise in sales prices for residential lumber, which exceeded the higher cost of lumber, improved pricing and volume gains for utility poles, partially offset by lower residential lumber demand.

For the first six months of 2021, gross profit grew to $309 million, or 20% of sales, compared to $214 million, or 17% of sales, in the corresponding period last year.

Selling and administrative

Selling and administrative expenses for the second quarter of 2021 amounted to $35 million, compared to $30 million in the prior year period, including depreciation and amortization of three million dollars in both periods. The increase in selling and administrative expenses is largely attributable to higher profit-sharing and stock-based compensation expense.

For the first six months of 2021, selling and administrative expenses amounted to $65 million, compared to $61 million in the prior year period, including depreciation and amortization of six million dollars in both periods.

Other losses, net

During the second quarter of 2021, other net losses were one million dollars, mainly related to a provision for the remediation of a site, offset in part by a foreign exchange gain. In the corresponding quarter of 2020, other net losses were minimal as a provision for the remediation of a site of five million dollars was largely offset by a favourable settlement of an environmental indemnification claim.

During the first six months of 2021, other net losses totaled one million dollars, compared to seven million in the corresponding period last year that essentially consisted of unrealized mark-to-market losses related to diesel and petroleum derivative commodity contracts. These commodity contracts expired at the end of 2020.

Financial expenses

Financial expenses amounted to six million dollars in the second quarter of 2021, down from seven million dollars in the corresponding period last year. The reduction in financial expenses is explained by lower interest rates, partially offset by higher year-over-year borrowings. For the first six months of 2021, financial expenses amounted to $12 million, down from $14 million for the same period last year.

Income before income taxes and income tax expense

During the second quarter of 2021, income before income taxes was $155 million, or 17% of sales, versus $94 million, or 12% of sales, in the corresponding period of 2020. The provision for income taxes totaled $40 million, compared to $25 million in the same period last year, representing an effective tax rate of approximately 26%.

For the six-month period ended June 30, 2021, income before income taxes was $231 million, or 15% of sales, versus $132 million, or 10% of sales in the corresponding period of 2020. The provision for income taxes totaled $60 million, compared to $35 million in the same period last year, representing an effective tax rate of approximately 26%.

Net income

Net income for the second quarter of 2021 was $115 million, or $1.76 per share, an increase of over 65% versus net income of $69 million, or $1.02 per share, in the corresponding period of 2020.

For the first six months of 2021, net income totaled $171 million, or $2.61 per share, an increase of over 75% compared with $97 million, or $1.43 per share, in the corresponding period last year.

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 ten quarters:

2021

For the quarters ended (in millions of dollars, except EPS)	**March 31**	**June 30**	**Sept. 30**	**Dec. 31**	**Total**
Sales	623	903			
EBITDA[(1)]	99	180			
Operating income	82	161			
Net income for the period	56	115			
EPS - basic and diluted	0.85	1.76			

2020

For the quarters ended (in millions of dollars, except EPS)	**March 31**	**June 30**	**Sept. 30**	**Dec. 31**	**Total**
Sales	508	768	742	533	2,551
EBITDA[(1)]	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 [(2)]	446	667	631	445	2,189
EBITDA[(1)]	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

(1) 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.

(2) Comparative figures have been adjusted to conform to the current period presentation.

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 June 30, 2021, compared to December 31, 2020 (see "Foreign Exchange" on page 7), results in a lower amount of assets and liabilities denominated in U.S. dollars, when expressed in Canadian dollars.

Assets

As at June 30, 2021, total assets stood at $2,602 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 from the consolidated statements of financial position.

Assets (in millions of dollars)	**As at June 30, 2021**	**As at December 31, 2020**	**Variance**
Accounts receivable	347	208	139
Inventories	1,120	1,075	45
Other current assets	35	36	(1)
Total current assets	**1,502**	**1,319**	**183**
Property, plant and equipment	571	574	(3)
Right-of-use assets	133	135	(2)
Intangible assets	117	115	2
Goodwill	273	280	(7)
Other non-current assets	6	3	3
Total non-current assets	**1,100**	**1,107**	**(7)**
Total assets	**2,602**	**2,426**	**176**

Accounts receivable, net of a credit loss allowance of less than one million dollar, were $347 million as at June 30, 2021, compared to $208 million as at December 31, 2020. The increase was attributable to the normal seasonal demand increase in the second quarter of 2021, when compared to the fourth quarter of 2020, amplified by strong sales in all three core product categories. 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 $1,120 million as at June 30, 2021, up from $1,075 million as at December 31, 2020. The increase is explained by higher fibre costs, particularly for residential lumber inventory given the significant rise in the market price of lumber, as well as, the higher level of residential lumber inventory, in part due to lower than expected sales volumes, partially offset by lower railway ties inventory and 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. Production is adjusted accordingly to optimize efficiency and capacity utilization.

Property, plant and equipment stood at $571 million as at June 30, 2021, compared with $574 million as at December 31, 2020. The slight decrease reflects the purchase of property, plant and equipment of $20 million during the first six months of 2021 offset by depreciation expense of $12 million for the period and the effect of currency translation of U.S. dollar denominated property, plant and equipment.

Right-of-use assets totaled $133 million as at June 30, 2021, compared to $135 million as at December 31, 2020. Additions of right-of-use assets, largely rolling stock, of $10 million during the first six months of the year were offset by depreciation expense of nine million dollars for the period and the effect of currency translation on U.S. dollar denominated right-of-use-assets.

Intangible assets and goodwill totaled $117 million and $273 million, respectively, as at June 30, 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 slightly primarily due to additions during the period, mainly for the implementation of a new enterprise resource planning (ERP) system, partially offset by amortization expense of six million dollars and the effect of currency translation on U.S.-based intangible assets. The decrease in goodwill is explained by the effect of currency translation on U.S.-based goodwill.

Liabilities

As at June 30, 2021, Stella-Jones' total liabilities stood at $1,156 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.

Liabilities (in millions of dollars)	**As at June 30, 2021**	**As at December 31, 2020**	**Variance**
Accounts payable and accrued liabilities	166	137	29
Current portion of long-term debt	63	11	52
Current portion of lease liabilities	34	33	1
Other current liabilities	37	37	—
Total current liabilities	**300**	**218**	**82**
Long-term debt	619	595	24
Lease liabilities	104	106	(2)
Other non-current liabilities	133	134	(1)
Total non-current liabilities	**856**	**835**	**21**
Total liabilities	**1,156**	**1,053**	**103**

Current liabilities were $300 million as at June 30, 2021, versus $218 million as at December 31, 2020. This variation is primarily attributable to a $52 million increase in current long-term debt, reflecting the reclassification of the US$50 million unsecured non-revolving term facility due in February 2022 to current portion of long-term debt. It also reflects a $29 million increase in accounts payable and accrued liabilities, in line with the increased business activity in the second quarter of 2021.

During the quarter, the Company repaid in full the total indebtedness outstanding under the demand loan facility, and terminated and canceled the facility. The borrowings under the demand loan facility were presented as short-term debt as at March 31, 2021.

In March 2021, the Company entered into a bridge term loan agreement with a lender within the U.S. farm credit system and a first installment of US$50 million was advanced and presented as short-term debt as at March 31, 2021. In April 2021, the second US$50 million installment was advanced and the US$100 million of indebtedness under the bridge loan facility was repaid in full.

During the second quarter of 2021, the Company entered into a credit agreement (the "U.S. Farm Credit Agreement") pursuant to which senior unsecured credit facilities of an aggregate amount of up to US$350 million were made available by a syndicate of lenders within the U.S. farm credit system. The U.S. Farm Credit Agreement provides a term loan facility of up to US$250 million with a delayed draw period of up to three years, and the choice of maturities of five to 10 years from the date of drawing, and a five-year revolving credit facility of up to US$100 million with a maturity date of April 29, 2026. A drawdown of $US100 million was made under the revolving credit facility and a $US100 million was borrowed under the term loan facility for seven years, maturing in June 2028. The proceeds from the revolving credit facility were used to repay in full the bridge term loan. The U.S. Farm Credit Agreement includes representations, warranties, covenants and events of default substantially similar to those under the existing syndicated credit agreement.

The Company's long-term debt, including the current portion, increased to $682 million as at June 30, 2021 versus $606 million as at December 31, 2020. The increase in borrowings was partially offset by the currency translation effect on U.S. dollar denominated long-term debt.

As at June 30, 2021, an amount of $209 million (US$169 million) was available against the Company's revolving credit facilities of $527 million (US$425 million) and $186 million (US$150 million) was available under the U.S. farm credit term loan facility.

As at June 30, 2021, the net debt to trailing 12-month EBITDA ratio decreased to 1.7x from 1.9x at the end of the fourth quarter of 2020. The Company was in full compliance with its debt covenants, reporting requirements and financial ratios as at June 30, 2021.

Shareholders' equity

Shareholders' equity stood at $1,446 million as at June 30, 2021, compared to $1,373 million as at December 31, 2020.

Shareholders' Equity (in millions of dollars)	**As at June 30, 2021**	**As at December 31, 2020**	**Variance**
Capital stock	211	214	(3)
Retained earnings	1,180	1,079	101
Accumulated other comprehensive income	55	80	(25)
Total shareholders' equity	**1,446**	**1,373**	**73**

The increase in shareholders' equity as at June 30, 2021 is attributable to net income of $171 million during the first six months of 2021. This increase was partially offset by a $52 million reduction in shareholders' equity related to the repurchase of shares, a $25 million decrease in accumulated other comprehensive income, mainly resulting from the currency translation of foreign operations, and $24 million of dividends.

On August 4, 2020, the TSX accepted Stella-Jones' Notice of Intention to Make a Normal Course Issuer Bid ("NCIB") to purchase for cancellation, up to 2,500,000 common shares during the 12-month period commencing August 10, 2020 and ending August 9, 2021. 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 June 30, 2021, the Company repurchased 296,307 common shares for cancellation in consideration of $14 million under its NCIB. For the six-month period ended June 30, 2021, the Company repurchased 1,097,568 common shares for cancellation in consideration of $51 million. Since the beginning of the NCIB on August 10, 2020, the Company repurchased a total of 2,429,023 common shares for cancellation in consideration of $111 million. As at June 30, 2021, the Company had unsettled transactions to repurchase 33,549 common shares for a cash consideration of one million dollars.

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 Periods Ended June 30,**		**Six-month Periods Ended June 30,**	
	2021	**2020**	**2021**	**2020**
Operating activities	173	146	32	53
Financing activities	(156)	(136)	(1)	(37)
Investing activities	(17)	(10)	(31)	(16)
Net change in cash and cash equivalents during the period	—	—	—	—
Cash and cash equivalents - Beginning of period	—	—	—	—
Cash and cash equivalents – End of period	—	—	—	—

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 operating activities

Cash flows from operating activities amounted to $173 million in the second quarter of 2021, compared to $146 million in the corresponding period in 2020, mainly due to improved profitability, partially offset by higher income tax installments in the quarter, given the delay of tax payments in 2020 permitted by COVID-19 tax relief measures. Cash flows from operating activities before changes in non-cash working capital components and interest and income taxes paid was $171 million in the second quarter of 2021, compared to $123 million in the corresponding period in 2020. Changes in non-cash working capital components increased liquidity by $37 million in the second quarter of 2021, primarily as a result of a seasonal decrease in inventories and an improvement in the days sales outstanding.

Cash flows from operating activities amounted to $32 million in the first six months of 2021, compared to $53 million in the corresponding period in 2020. The improved profitability in 2021 was offset by a greater increase in working capital compared to the same period last year, largely stemming from higher fibre costs and the timing of income tax installments given COVID-19 tax relief measures in 2020. Cash flows from operating activities before changes in non-cash working capital components and interest and income taxes paid was $271 million in the first six months of 2021, compared to $192 million in the corresponding period in 2020. Changes in non-cash working capital components decreased liquidity by $176 million in the first six months of 2021, primarily attributable to an increase in accounts receivable and inventories which exceeded the increase in accounts payable and accrued liabilities.

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 operating activities (in millions of dollars)	**Three-month Periods Ended June 30,**		**Six-month Periods Ended June 30,**	
	2021	**2020**	**2021**	**2020**
Net income	115	69	171	97
Depreciation and amortization	19	19	36	37
Current income taxes expense	37	21	59	33
Other	—	14	5	25
Cash flows from operating activities before changes in non-cash working capital components and interest and income taxes paid	**171**	**123**	**271**	**192**
Accounts receivable	27	(89)	(144)	(183)
Inventories	36	105	(63)	19
Other current assets	(1)	(5)	1	(5)
Accounts payable and accrued liabilities	(25)	18	30	45
Changes in non-cash working capital components	**37**	**29**	**(176)**	**(124)**
Interest paid	(3)	(5)	(11)	(13)
Income taxes paid	(32)	(1)	(52)	(2)
Cash flows from operating activities	**173**	**146**	**32**	**53**

Cash flows used in financing activities

Financing activities for the second quarter of 2021 decreased cash by $156 million. During the quarter ended June 30, 2021, the Company repaid in full its short-term debt and decreased its borrowings under the revolving credit facilities by $84 million, while increasing its long-term debt by $110 million. In addition, the Company paid dividends of $24 million and repurchased shares for $14 million. In the second quarter of 2020, financing activities decreased cash by $136 million, primarily due to the repayment of $99 million under its revolving credit facilities, five million of its long-term debt and the payment of dividends of $20 million.

For the first six months of 2021, financing activities reduced cash by one million dollars, compared to $37 million for the same period in 2020.

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 used in financing activities (in millions of dollars)	**Three-month Periods Ended June 30,**		**Six-month Periods Ended June 30,**	
	2021	**2020**	**2021**	**2020**
Increase (decrease) in short-term debt	(134)	—	3	—
Net change in revolving credit facilities	(84)	(99)	42	9
Increase (decrease) in long-term debt	110	(5)	47	(6)
Dividends on common shares	(24)	(20)	(24)	(20)
Repurchase of common shares	(14)	—	(51)	—
Other	(10)	(12)	(18)	(20)
Cash flows used in financing activities	**(156)**	**(136)**	**(1)**	**(37)**

Cash flows used in investing activities

Investing activities used $17 million of cash flows in the second quarter of 2021, compared to $10 million in the second quarter of 2020, explained by the purchase of property, plant and equipment as well as expenditures related to the implementation of the ERP system.

For the first six months of 2021, the Company invested $31 million, compared to $16 million for the corresponding period in 2020, primarily explained by the purchase of property, plant and equipment.

The following table provides information on cash flows used in investing activities from the consolidated statements of cash flows.

Cash flows used in investing activities (in millions of dollars)	**Three-month Periods Ended June 30,**		**Six-month Periods Ended June 30,**	
	2021	**2020**	**2021**	**2020**
Purchase of property, plant and equipment	(10)	(8)	(20)	(13)
Additions of intangible assets	(6)	(3)	(10)	(4)
Other	(1)	1	(1)	1
Cash flows used in investing activities	**(17)**	**(10)**	**(31)**	**(16)**

Financial obligations

The following table details the maturities of the financial obligations as at June 30, 2021:

Financial obligations (in millions of dollars)	**Carrying Amount**	**Contractual Cash flows**	**Less than 1 year**	**Years 2-3**	**Years 4-5**	**More than 5 years**
Accounts payable and accrued liabilities	166	166	166	—	—	—
Long-term debt obligations [(1)]	682	745	17	124	383	221
Minimum payments under lease liabilities	138	152	38	54	29	31
Derivative financial instruments	2	2	2	2	(1)	(1)
Financial obligations	**988**	**1,065**	**223**	**180**	**411**	**251**

(1) Includes interest payments. Interest on variable interest debt is assumed to remain unchanged from the rates in effect as at June 30, 2021.

SHARE AND STOCK OPTION INFORMATION

As at June 30, 2021, the capital stock issued and outstanding of the Company consisted of 65,105,179 common shares (66,187,404 as at December 31, 2020).

The following table presents the outstanding capital stock activity for the three-and six-month periods ended June 30, 2021:

Number of shares	Three-month Period Ended June 30, 2021	Six-month Period Ended June 30, 2021
Balance – Beginning of year	65,392,450	66,187,404
Common shares repurchased	(296,307)	(1,097,568)
Employee share purchase plans	9,036	15,343
Balance – End of period	**65,105,179**	**65,105,179**

As at August 2, 2021, the capital stock issued and outstanding consisted of 64,765,496 common shares.

As at June 30, 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 August 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 July 30, 2021, the Company obtained a one-year extension of its unsecured syndicated revolving credit facility to February 27, 2026. The extension was granted through an amendment to the sixth amended and restated credit agreement dated as of May 3, 2019. All terms and conditions remain substantially unchanged.

On August 2, 2021 the Board of Directors declared a quarterly dividend of $0.18 per common share payable on September 17, 2021 to shareholders of record at the close of business on September 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 risk 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 June 30, 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 effectively designed, as at June 30, 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 April 1, 2021 to June 30, 2021 that have materially affected or are reasonably likely to materially affect the Company's ICFR.

UPDATED OUTLOOK

The Company has revised its full-year financial forecast to reflect the softening of residential lumber demand in the second half of 2021. Stella-Jones continues to foresee solid EBITDA growth in 2021 compared to 2020 but expects EBITDA to be in the range of $410 to $440 million, compared to the previously disclosed guidance of $450 to $480 million. The margin expansion realized in the first half of 2021 is projected to offset the margin compression expected from declining market prices of lumber until the Company averages down its higher cost of inventory. As a result, the Company anticipates EBITDA margin as a percentage of sales for 2021 to remain comparable to 2020.

Excluding the impact of the currency conversion, the Company is projecting sales growth in the low-to-high teens for 2021 compared to 2020, down from the projected increase of 15% to low 20% previously disclosed. The decrease in the sales growth projection largely stems from the expected slowdown in consumer demand for residential lumber. Residential lumber sales are expected to increase 15% to 20% compared to 2020, down from the previously disclosed forecasted increase of 45% to 65%. While the sales growth forecast for utility poles remains unchanged with a high-single digit increase compared to 2020, railway ties and industrial products sales are projected to increase in the low-single digit range. For railway ties, the current pricing headwinds are expected to ease by the end of the year and the Company believes it will continue to benefit from increased maintenance activity.

This updated guidance anticipates a reduction of approximately $130 million in sales from the depreciation of the value of the U.S. dollar relative to the Canadian dollar to C$1.25 per U.S. dollar.

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

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

- 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;
- Canadian dollar will trade, on average, at approximately C$1.25 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.

August 2, 2021