MANAGEMENT'S DISCUSSION & ANALYSIS

Three-month period ended June 30, 2009 compared with three-month period ended June 30, 2008

The following Management's Discussion and Analysis ("MD&A") and the Company's interim unaudited consolidated financial statements were approved by the Audit Committee and the Board of Directors on August 12, 2009. The MD&A provides a review of the significant developments and results of operations of the Company during the three-month period ended June 30, 2009 compared with the three-month period ended June 30, 2008. The MD&A should be read in conjunction with the Company's interim unaudited consolidated financial statements for the periods ended June 30, 2009 and 2008 and the notes thereto. The interim financial statements are prepared in accordance with Canadian Generally Accepted Accounting Principles and results are reported in Canadian dollars.

The MD&A contains statements that are forward-looking in nature. Such statements 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, product selling prices, raw material and operating costs, changes in foreign currency rates and other factors referenced herein and in the Company's continuous disclosure filings.

Additional information, including the Company's Annual Information Form, quarterly and annual reports, and supplementary information is available on SEDAR at www.sedar.com. Press releases and other information are also available in the Investor/Media Centre section of the Company's Web site at www.stella-jones.com.

OUR BUSINESS

Stella-Jones is a leading North American producer and marketer of industrial pressure treated wood products and also provides treated consumer lumber products and customized services to lumber retailers and wholesalers for outdoor applications.

The Company specializes in four major product categories: railway ties for rail transportation companies; treated wood utility poles for utility and telecommunication companies; industrial lumber products for construction and maritime applications, and treated consumer lumber products for the residential market.

As of August 12, 2009, the Company owns and operates fifteen wood treating plants, two distribution centres, two pole peeling facilities and has a 50% interest in a third pole peeling operation. These twenty facilities are located in six Canadian provinces and seven American states. The Company's workforce currently numbers approximately 735 employees.

Stella-Jones enjoys a number of key attributes which should further enhance the Company's strategic positioning and competitive advantage in the wood treatment industry. Among these are the ability to service clients from multiple plants, a solid financial position that allows the Company to stockpile and air-season green wood for major long-term contracts, and a long-standing stable source of wood supply. Stella-Jones also operates dedicated production facilities which result in higher productivity and better efficiency, helping to preserve a competitive manufacturing cost structure.

OUR MISSION

Stella-Jones' objective is to be the performance leader in the wood preserving industry and a model corporate citizen, exercising environmental 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 and productive environment for its employees, where problem solving, initiative and high standards of performance are rewarded.

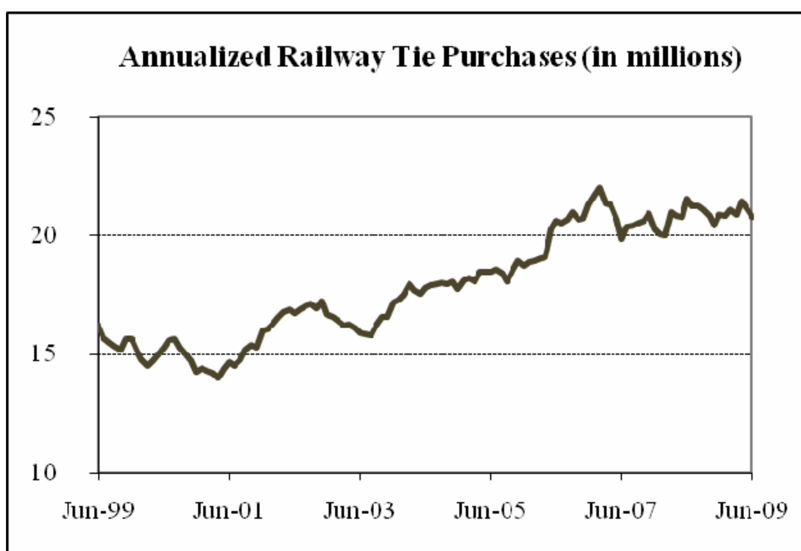
FOREIGN EXCHANGE

The table below shows exchange rates applicable to the quarters ended June 30, 2009 and 2008. Average rates are used to translate sales and expenses for the periods mentioned, while closing rates translate assets and liabilities of self-sustaining foreign operations and monetary assets and liabilities of the Canadian operations.

Cdn$/US$	2009		2008	
	Average	Closing	Average	Closing
Second Quarter	1.1820	1.1630	1.0110	1.0197

INDUSTRY OVERVIEW

Railway ties



Source: Railway Tie Association

As reported by the Railway Tie Association, railway tie purchases decelerated slightly in the second quarter of 2009. As at June 30, the annualized purchase rate stood at 20.8 million ties, a level that remains healthy by historical standards, as shown in the accompanying chart.

This deceleration reflects a more prudent approach by railway operators, as a weaker economy has reduced the volume of freight hauled on North American railways in the past year, according to data published by the Association of American Railroads.

OPERATING RESULTS

Sales

Sales for the quarter ended June 30, 2009 reached $129.1 million, an increase of $6.0 million, or 4.9%, over last year's second quarter sales of $123.1 million. This increase is essentially attributable to the weakness in the value of the Canadian dollar, Stella-Jones' reporting currency, versus the U.S. dollar, which increased the value of U.S. dollar denominated sales by about $10.2 million. Factoring out the foreign exchange effect, sales declined approximately 3.0%, reflecting lower demand in the Company's railway tie product category.

Sales for the six-month period ended June 30, 2009 totalled $241.1 million, up $51.8 million, or 27.4%, from sales of $189.3 million in the first six months of 2008. This increase includes the contribution of $37.3 million from the operations of The Burke-Parsons-Bowlby Corporation ("BPB"), acquired on April 1, 2008. In addition, the weakness of the Canadian dollar versus the U.S. currency increased the value of U.S. dollar denominated sales by about $16.9 million when compared with the previous year.

Sales by product group

Railway ties

Railway tie sales for the second quarter of 2009 amounted to $57.6 million, a decrease of 8.3% over sales of $62.8 million in the second quarter of 2008. These results primarily reflect a one-time export sale in 2008, lower overall market demand during the period and competitive pricing. Railway tie sales accounted for 44.6% of the Company's total sales in the second quarter of 2009, versus 51.0% in the corresponding quarter last year. For the first six months of 2009, railway tie sales were $118.9 million, up from $95.1 million in the corresponding period of 2008, reflecting a six-month contribution from BPB versus only three months last year.

Utility poles

Utility pole sales stood at $44.2 million in the second quarter of 2009, an increase of $7.2 million, or 19.5%, over sales of $37.0 million in the same period last year. The year-over-year revenue growth was mainly driven by solid demand for transmission poles in the United States, greater market penetration by the Company's sales force, and a higher conversion rate on U.S. dollar denominated utility pole sales. Utility pole sales accounted for 34.2% of the Company's total sales in the second quarter of 2009, versus 30.1% in the corresponding quarter last year. For the six-month period ended June 30, 2009, sales of utility poles totalled $81.7 million, up from $64.7 million a year ago.

Industrial lumber

Industrial lumber sales reached $11.9 million in the second quarter of 2009, compared with $10.3 million a year earlier. The 15.0% sales increase is mainly related to strong demand for marine applications in Canada. The category represented 9.2% of overall sales in the second quarter of 2009. For the first six months of 2009, industrial lumber sales were $22.3 million compared with $12.4 million in 2008, reflecting the added contribution from BPB for the full period.

Consumer lumber

Sales in the consumer lumber category totalled $15.5 million in the second quarter of 2009, up 19.3% from $13.0 million for the corresponding period in 2008. The increase is attributable to more retail points of sale compared with a year ago as well as robust demand partly driven by the home renovation tax credit program in Canada. The Company does not sell consumer lumber into the U.S. market. Consumer lumber accounted for 12.0% of Stella-Jones' total sales in the second quarter of 2009. For the first half of 2009, consumer lumber sales amounted to $18.2 million compared with $17.1 million in the corresponding period of 2008.

Sales by destination

In the second quarter of 2009, sales in Canada grew 3.4% to $59.4 million, or 46.0% of the Company's total sales. Sales in the United States amounted to $69.7 million, or 54.0% of sales, an increase of $4.1 million, or 6.2%, over the second quarter of 2008, entirely owing to a higher conversion rate on U.S. dollar denominated sales.

For the first six months of 2009, sales in Canada reached $100.4 million, representing 41.7% of sales, up from $95.8 million a year ago, while sales in the United States amounted to $140.6 million, or 58.3% of sales, versus $93.5 million in the corresponding period of 2008.

Gross profit

Gross profit reached $23.9 million or 18.5% of sales in the second quarter of 2009, down from $25.3 million or 20.6% of sales in the second quarter of 2008. The decrease in gross profit, both in dollars and as a percentage of sales, essentially stems from lower margins on railway tie sales as a result of competitive pricing in response to softer industry demand and, to a lesser extent, lower margins on U.S. utility pole sales. Cost of sales for the second quarter of 2009 also includes a $511,600 provision for plant closure and workforce reductions (see Capacity Optimization Measures below). Excluding this provision, gross profit would have been $24.4 million, or 18.9% of sales.

For the six-month period ended June 30, 2009, gross profit was $46.4 million, or 19.3% of sales, compared with $39.2 million, or 20.7% of sales, for the six-month period ended June 30, 2008.

Expenses

Selling and administrative expenses amounted to $5.3 million in the second quarter of 2009, down from $5.9 million in the corresponding period of 2008. As a percentage of sales, selling and administrative expenses represented 4.1% of sales in the second quarter of 2009, compared with 4.8% in the prior year. This decrease in dollars and as a percentage of sales reflects overall cost containment and reduced compensation expenses.

For the first six months of 2009, selling and administrative expenses totalled $11.1 million, or 4.6% of sales, compared with $8.8 million, or 4.6% of sales, in the corresponding period of 2008.

The Company realized a foreign exchange gain of $271,000 for the quarter ended June 30, 2009, as opposed to a foreign exchange loss of $14,000 last year. For the six-month period ended June 30, 2009, the realized foreign exchange gain stood at $278,000, versus a gain of $161,000 a year ago.

The Company's exposure to foreign exchange gains or losses from currency fluctuations is related to its sales and purchases in U.S. dollars by its Canadian based operations. Stella-Jones U.S. Holding Corporation, the Company's wholly-owned U.S. subsidiary, is a self-sustaining foreign operation and unrealized foreign exchange gains and losses on translating its financial statements are deferred in shareholders' equity. The Company monitors its transactions in U.S. dollars generated by Canadian based operations. Its basic hedging activity for economic purposes consists of entering into forward foreign exchange contracts for the sale of U.S. dollars and purchasing certain goods and services in U.S. dollars. The Company will also consider forward foreign exchange contracts for the purchase of U.S. dollars for significant purchases of goods and services that are not covered by natural hedges. On June 30, 2009, the Company had on hand forward foreign exchange contracts for the future sale of US$18.8 million at an average contract rate of Cdn$1.2278/US$1.00. The non-cash gain on these forward foreign exchange contracts resulting from the change in their mark-to-market values as at June 30, 2009, compared to March 31, 2009, totalled $2.1 million, whereas the non-cash gain from the change compared to December 31, 2008, was $1.2 million.

Amortization of capital and intangible assets totalled $2.5 million in the second quarter of 2009, an increase of $0.7 million over the same period in 2008. This increase reflects higher capital assets following recent purchases as well as a less favourable exchange rate on the amortization of U.S. based capital and intangible assets. For the first six months of 2009, amortization of capital and intangible assets amounted to $5.1 million, up from $3.4 million in the corresponding period of 2008.

Financial expenses for the second quarter of 2009 were unchanged from a year ago at $2.3 million. However, increases in long- and short-term borrowings resulting from the BPB acquisition and working capital requirements, respectively, were somewhat offset by lower interest rates, on average, in 2009. After the first six months of 2009, financial expenses reached $4.5 million versus $3.7 million in the corresponding period of 2008.

Earnings before income taxes and income tax expense

Stella-Jones generated earnings before income taxes of $16.2 million, or 12.5% of sales, in the second quarter of 2009, representing an increase of $0.8 million over earnings before income taxes of $15.3 million, or 12.4% of sales, in the second quarter of 2008.

Stella-Jones' income tax expense totalled $5.1 million in the second quarter of 2009, representing an effective tax rate of 31.8%. In the corresponding period of 2008, the income tax expense stood at $5.3 million, equivalent to an effective tax rate of 34.4%. The lower effective tax rate is a consequence of the higher proportion of revenue generated in the United States that is subject to the domestic manufacturing tax deduction for qualifying manufacturing income and deductions for Canadian income tax related to dividends received from a related party. Other non-income based corporate taxes represent a relatively small component of the Company's total tax burden.

For the first six months of 2009, earnings before income taxes amounted to $27.3 million, or 11.3% of sales, compared to $23.5 million, or 12.4% of sales, in the first six months of 2008. The income tax expense totalled $8.6 million, representing an effective tax rate of 31.6%, compared with an income tax expense of $8.2 million, equivalent to an effective tax rate of 34.7% in the corresponding period of 2008.

Net earnings

Net earnings for the three-month period ended June 30, 2009 totalled $11.0 million, or $0.87 per share, fully diluted, compared with $10.0 million, or $0.80 per share, fully diluted, in the second quarter of 2008. This represents a year-over-year increase in net earnings of 9.7%. For the six-month period ended June 30, 2009, net earnings reached $18.7 million, or $1.48 per share, fully diluted, versus net earnings of $15.4 million, or $1.21 per share, fully diluted, in the corresponding period of 2008.

CAPACITY OPTIMIZATION MEASURES

As part of the Company's continuous monitoring of operating cost efficiency, Management proactively reviews capacity utilization across Stella-Jones' continental plant network to ensure such utilization is optimized. In this regard, the Company has decided to close its Stanton, Kentucky facility at the end of business on September 4, 2009. This will result in the termination of ten employees. Production, consisting essentially of treated wood for custom log homes and highway timbers, will be transferred to the Company's Spencer, West Virginia facility. Furthermore, the workforce at the Spencer facility will be reduced by 29 employees effective August 13, 2009 as the Company will be shifting the majority of Spencer's railway tie production to its other plants.

To cover the costs related to the closure and employee reductions, the Company has taken a provision of $511,600 (US$468,600). This provision is included in the Company's cost of sales for the three- and six-month periods ended June 30, 2009.

QUARTERLY RESULTS

The Company's sales have historically followed a seasonal pattern, with railway tie, utility pole and industrial lumber shipments strongest in the second and third quarters to provide industrial end users with product for their summer maintenance projects. Consumer lumber sales also follow a similar seasonal pattern. In the fall and winter seasons, there tends to be less activity; thus the first and fourth quarters are typically characterized by relatively lower sales levels.

2009

For the quarters ended	**March 31**	**June 30**			
(thousands of dollars, except per share data)	**$**	**$**			
Sales	111,954	129,104			
Operating earnings before amortization of capital and intangible assets [1]	15,924	20,976			
Operating earnings [1]	13,313	18,475			
Net earnings for the period	7,687	11,021			
Net earnings per common share					
Basic	0.61	0.87			
Diluted	0.61	0.87			

2008

For the quarters ended	**March 31**	**June 30**	**Sept. 30**	**Dec. 31**	**Total**
(thousands of dollars, except per share data)	**$**	**$**	**$**	**$**	**$**
Sales	66,182	123,081	111,828	83,731	384,822
Operating earnings before amortization of capital and intangible assets [1]	11,199	19,402	14,249	13,479	58,329
Operating earnings [1]	9,616	17,599	12,127	10,622	49,964
Net earnings for the period	5,323	10,047	6,850	6,327	28,547
Net earnings per common share					
Basic	0.43	0.81	0.55	0.50	2.29
Diluted	0.42	0.80	0.54	0.50	2.25

2007

For the quarters ended	**March 31**	**June 30**	**Sept. 30**	**Dec. 31**	**Total**
(thousands of dollars, except per share data)	**$**	**$**	**$**	**$**	**$**
Sales	61,949	84,510	74,815	48,439	269,714
Operating earnings before amortization of capital and intangible assets [1]	12,301	14,725	13,254	9,219	49,500
Operating earnings [1]	11,235	13,424	11,864	7,537	44,060
Net earnings for the period	6,097	8,078	7,085	4,440	25,700
Net earnings per common share					
Basic	0.50	0.66	0.57	0.36	2.09
Diluted	0.48	0.64	0.56	0.35	2.03

1 Operating earnings before amortization of capital and intangible assets and operating earnings are financial measures not prescribed by Canadian generally accepted accounting principles (“GAAP”) and are not likely to be comparable to similar measures presented by other issuers. Management considers they represent useful information for comparison with other similar operations in our industry, as they present financial results related to industry practice, not affected by non-cash charges or capital structure. Operating earnings before amortization of capital and intangible assets and operating earnings are readily reconcilable to net earnings presented in our Canadian GAAP financial statements, as there are no adjustments for unusual or non-recurring items.

Note: due to rounding, the sum of results for the quarters may differ slightly from the total shown for the full year.

BALANCE SHEET

The Company’s working capital at June 30, 2009 was $171.0 million, an increase of $14.1 million over the working capital balance of $156.9 million at December 31, 2008. The value of current assets increased $21.5 million during the first half of 2009, essentially reflecting a $19.3 million increase in accounts receivable as a result of the normal seasonal demand pattern. Inventories stood at $225.9 million, relatively stable from $223.2 million at December 31, 2008, but down from $243.3 million at the end of the first quarter owing to seasonal demand pattern and local currency depreciation on U.S. based inventories during the second quarter.

Because of 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. However, solid relationships and long-term contracts with certain customers enable the Company to better ascertain inventory requirements. The Company believes that its cash flow from operations and available operating lines of credit are adequate to meet its working capital requirements for the foreseeable future.

Capital assets stood at $104.8 million as at June 30, 2009, compared with $108.8 million as at December 31, 2008. This $4.0 million decrease is related to local currency depreciation on U.S. based capital assets and to the amortization expense exceeding purchases of capital assets since December 31, 2008.

Intangible assets totalling $15.4 million, comprised of customer relationships and the discounted value of the non-compete agreements, as well as goodwill of $6.1 million, were included in the Company's balance sheet as at June 30, 2009.

Bank indebtedness as at June 30, 2009 stood at $84.9 million, compared with $81.6 million at the end of December 2008. This increase essentially mirrors higher working capital requirements. However, strong cash flow generation and the effect of local currency depreciation on the Company's U.S. operating lines of credit during the second quarter reduced bank indebtedness by more than $15.0 million over that period.

Bank indebtedness includes a $50.0 million demand operating loan with a Canadian bank as well as a US$45.0 million (Cdn$52.3 million) operating line of credit with the U.S. bankers of Stella-Jones' U.S. subsidiaries. Total availability under the Company's Canadian and U.S. operating lines of credit was $11.4 million and US$10.3 million (Cdn$12.0 million), respectively, as at June 30, 2009.

The Company believes that these operating lines of credit, combined with its funds from operations in the next quarters, will be adequate to meet its cash requirements for the foreseeable future. However, future acquisitions, if any, may require new sources of financing.

As at June 30, 2009, the Company's long-term debt, including the current portion, amounted to $99.8 million, down from $105.8 million as at December 31, 2008. This decrease is due to a lower conversion rate of U.S. dollar denominated long-term debt into Canadian currency as well as to repayment of $2.8 million in long-term debt during the first six months of 2009.

Shareholders' equity was $175.5 million as at June 30, 2009, a $14.4 million increase from December 31, 2008 levels. The Company's strong earnings generation accounted for most of this gain. Book value stood at $13.85 per common share as at June 30, 2009, up from $12.82 per share at the end of last year.

LIQUIDITY AND CAPITAL RESOURCES

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

Summary of cash flows	**Three-month periods ended**		**Six-month periods ended**	
(thousands of dollars)	**June 30, 2009**	**June 30, 2008**	**June 30, 2009**	**June 30, 2008**
Operating activities	$14,668	$9,753	$2,142	($4,688)
Financing activities	($14,653)	$30,569	($21)	$45,625
Investing activities	($15)	($40,322)	($2,121)	($40,937)
Cash and cash equivalents	$---	$---	$---	$---

The Company's activities, acquisitions and capital expenditures are primarily financed by cash flows from operating activities and the use of cash and operating lines of credit. The Company's operating lines of credit are demand operational facilities that are renewable annually and are subject to review by the Company's bankers at intervals no greater than one year. In the first quarter of 2009, the Company's Canadian bankers amended the interest rate structure with no change to the available amount of the operating facility and approved an increase to the credit availability for the purchase of forward foreign exchange contracts. The Company anticipates no difficulties in its ability to renew these demand operating facilities.

Cash flow from operating activities before changes in non-cash working capital components was $12.6 million for the three-month period ended June 30, 2009, compared with $12.4 million for the prior year. This 1.3% increase reflects higher net earnings and non-cash amortization charges. For the six-month period ended June 30, 2009, cash flow from operating activities before changes in non-cash working capital components reached $23.9 million, up from $19.8 million in the corresponding period of 2008.

Changes in non-cash working capital components provided liquidity of $2.1 million versus a liquidity requirement of $2.7 million for the three-month period a year ago. This improvement essentially mirrors reduced inventories somewhat offset by a reduction in accounts payable and accrued liabilities. As a result, operating activities increased liquidity by $14.7 million for the three-month period ended June 30, 2009, compared with $9.8 million a year earlier. For the six-month period ended June 30, 2009, cash flows from operating activities provided liquidity of $2.1 million, as opposed to requiring liquidity of $4.7 million in the first six months of 2008.

Cash flows used for financing activities amounted to $14.7 million for the quarter ended June 30, 2009, mainly as a result of an $11.5 million reduction in bank indebtedness and $2.3 million in dividends paid to common shareholders. Financing activities had provided liquidity of $30.6 million for the same period a year prior. For the six-month period ended June 30, 2009, cash flows from financing activities used liquidity of $21,000, as opposed to providing funds of $45.6 million a year earlier.

Investing activities required $15,000 in cash during the second quarter of 2009, versus requiring $40.3 million in the second quarter of 2008. For the first six months of 2009, cash flows used for investing activities reduced liquidity by $2.1 million compared with a reduction of $40.9 million in 2008.

The Company's contractual obligations for future payments are outlined in the table below:

Payments due by period (in thousands of dollars)	**Less than 1 year ($)**	**1 – 3 years ($)**	**4 – 5 years ($)**	**After 5 years ($)**	**Total ($)**
Bank indebtedness	84,937	-	-	-	84,937
Accounts payable and accrued liabilities	34,850	-	-	-	34,850
Long-term debt obligations	4,956	11,951	22,371	61,635	100,913
Interest on long-term debt obligations	5,544	10,065	7,804	7,791	31,204
Operating leases and other contractual obligations	3,165	4,619	2,353	10,263	20,400
Capital lease obligations	109	169	259	945	1,482
Interest on capital lease obligation	72	121	101	68	362
Foreign exchange forward contracts					
Outflow	4,361	-	-	-	4,361
Inflow	(4,334)	-	-	-	(4,334)
Non-compete agreements	1,454	2,908	2,543	-	6,905
Total	135,114	29,833	35,431	80,702	281,080

SHARE AND STOCK OPTION INFORMATION

As at June 30, 2009, the capital stock issued and outstanding consisted of 12,677,175 common shares (12,564,925 as at December 31, 2008). As at August 12, 2009, the capital stock issued and outstanding consisted of 12,677,175 common shares.

As at June 30, 2009, the number of outstanding options to acquire common shares issued under the Company's Stock Option Plan was 140,785 (December 31, 2008 – 147,785) of which 89,285 (December 31, 2008 – 93,285) were exercisable. As at August 12, 2009, the number of outstanding options was 140,785, of which 98,285 were exercisable.

Effective May 6, 2003, the Company granted to its President and Chief Executive Officer, under a Stock Option Agreement, 300,000 options to acquire an equivalent number of common shares at an exercise price of $2.99 per share. These options became exercisable on May 6, 2008 and all options have been exercised as at August 12, 2009.

DIVIDENDS

On August 12, 2009, the Board of Directors declared a semi-annual dividend of $0.18 per common share payable on October 9, 2009. The declaration, amount and date of any future dividends will continue to be considered by the Board of Directors of the Company based upon and subject to the Company's earnings and financial requirements, covenants in its loan documentation and other conditions prevailing at the time. There can be no assurance as to the amount or timing of such dividends in the future.

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 2008 Annual Report.

CURRENT ECONOMIC CONDITIONS

In light of weaker economic and financial markets conditions, the Company continues to carefully monitor its strategy and risk management. Although financial results remain positive, the economic climate is prompting Management to take a more cautious approach in executing its business strategy.

Operations

Tighter credit market conditions have resulted in the deferral or cancellation of certain projects, especially in alternative energy, for which some of the Company's products could be required. Such projects include ethanol plants and wind farms, which both have significant capital requirements. In recent years, the Company has supplied railway ties to link up ethanol plants with the continental rail network and utility poles to connect wind farms with the electricity transmission grid. As at August 12, 2009, Stella-Jones has not been materially affected by such deferrals or cancellations.

Though not recession proof, the Company's core utility pole and railway tie product categories are integral to capital infrastructure projects that governments often initiate during times of economic slowdown. Therefore, the Company's position as a supplier of utility poles and railway ties could prove particularly advantageous given the American and Canadian governments' stated intention to invest heavily in infrastructure projects. Moreover, various U.S. tax credit initiatives, whether enacted into law or proposed, could prove a significant stimulus for infrastructure projects. As at August 12, 2009, Stella-Jones has not been materially affected by such stimulus proposals.

Liquidity

As at June 30, 2009, the Company is in full compliance with its debt covenants and contractual obligations. In addition, it has total availability under its Canadian and U.S. operating lines of credit of $11.4 million and US$10.3 million, respectively, as at June 30, 2009.

Management considers that substantially all receivables are fully collectible as major customers, mainly Class 1 railroad operators and large-scale utility service providers, have good credit standing and limited history of default. Nevertheless, Management is providing additional focus on accounts receivable collection and credit extensions.

Inventories decreased during the second quarter of 2009 as a result of normal seasonal demand patterns. To ensure efficient treatment operations, given that air-dried wood reduces treatment cycles, inventory turnover has historically been relatively low. Nevertheless, Management continuously monitors the levels of inventory and market demand for its products. Production is adjusted accordingly to optimize efficiency and capacity utilization.

RISKS AND UNCERTAINTIES

The risk and uncertainty factors affecting the Company in the future remain substantially unchanged from those included in the Company's annual MD&A contained in its 2008 Annual Report.

SIGNIFICANT ACCOUNTING POLICIES

The Company's significant accounting policies are described in Note 1 to the June 30, 2009, interim unaudited consolidated financial statements.

The Company prepares its consolidated financial statements in conformity with Canadian generally accepted accounting principles which require Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reported periods. 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 earnings in the period in which they become known.

Significant items subject to estimates and assumptions include the estimated useful life of assets, impairment of long-lived assets, future income taxes, stock-based compensation, pension and post retirement benefits, legal liabilities, bad debts, allowance for doubtful accounts and environmental provisions.

CHANGES IN ACCOUNTING POLICIES

The Canadian Institute of Chartered Accountants ("CICA") issued the following new accounting standard which was adopted by the Company effective January 1, 2009:

- Handbook Section 3064, "Goodwill and Intangible Assets", replaces Section 3062 "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". Section 1000, "Financial Statements Concepts" was amended accordingly to Section 3064. This new Section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit oriented companies. The Company has assessed that the impact of this new accounting standard is not significant. Additionally, the new required disclosures have been included in Note 3 to the June 30, 2009 interim unaudited consolidated financial statements.

On January 20, 2009, the Emerging Issues Committee ("EIC") of the Canadian Accounting Standards Board ("AcSB") issued EIC Abstract 173, "Credit Risk and Fair Value of Financial Assets and Financial Liabilities", which establishes that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. EIC Abstract 173 should be applied retrospectively without restatement of prior years to all financial assets and liabilities measured at fair value in interim and annual financial statements for periods ending on or after January 20, 2009. The Company has assessed that the impact of EIC Abstract 173 is not significant.

IMPACT OF ACCOUNTING PRONOUNCEMENTS NOT YET IMPLEMENTED

The CICA issued the following accounting standards which will be adopted by the Company effective January 1, 2011:

- Handbook Section 1582, "Business Combinations", which replaces Section 1581, "Business Combinations". The Section establishes standards for the accounting for a business combination. It provides the Canadian equivalent to the IFRS standard, IFRS 3 (Revised), "Business Combinations". The Section applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Earlier application is permitted. The Company is currently evaluating the impact of the adoption of this new accounting standard on the consolidated financial statements.

- Handbook Section 1601, "Consolidated Financial Statements", and Section 1602, "Non-controlling Interests", which together replace Section 1600, "Consolidated Financial Statements". Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of IFRS standard, IAS 27 (Revised), "Consolidated and Separate Financial Statements". Earlier adoption is permitted as of the beginning of a fiscal year. The Company is currently evaluating the impact of the adoption of these new accounting standards on the consolidated financial statements.

INTERNATIONAL FINANCIAL REPORTING STANDARDS

In February 2008, the AcSB confirmed that Canadian publicly listed companies will be required to use International Financial Reporting Standards ("IFRS") in the preparation of financial statements for fiscal years beginning on or after January 1, 2011.

The Company will be required to use IFRS for the interim and annual financial statements dated after January 1, 2011, although this transition date will require the restatement of comparative figures reported for the year ended December 31, 2010.

Management has established an IFRS implementation team to develop an IFRS changeover plan. In 2008, a preliminary diagnostic analysis was prepared by external consultants. This process is presently in the phase 2 stage, which includes a definition of roles and responsibilities, a review of the differences between current Canadian GAAP (as applied by the Company) and IFRS, and the analysis of possible options regarding adoption. Once this stage is complete, Management will be able to determine the exact consequences of the change. Planning continued in the second quarter of 2009 to precisely establish the changes to be made to accounting principles and computer systems, training requirements, internal control mechanisms for financial reporting and the repercussions on the Company's business activities. The financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

DISCLOSURE CONTROLS AND INTERNAL CONTROL OVER FINANCIAL REPORTING

In accordance with the Canadian Securities Administrators' National Instrument 52-109 (Certification of Disclosure in Issuer's Annual and Interim Filings), the Company has filed certificates signed by the President and Chief Executive Officer and the Senior Vice-President and Chief Financial Officer that, among other things, report on the design of disclosure controls and procedures and on the design of internal control over financial reporting.

The Company did not make any material changes to the design of internal controls over financial reporting during the three months ended June 30, 2009 that have had a material effect on the Company's internal controls over financial reporting.

OUTLOOK

The global economic situation calls for a cautious outlook, as evidenced by short-term challenges caused by softer demand and price competition, which have slightly reduced the Company's organic sales growth and profitability. In light of this context, Management is continuously reviewing cost efficiency in its operations and optimizing capacity utilization across its continental plant network. The planned closure of the Stanton, Kentucky facility and rationalization of the Spencer, West Virginia facility are in keeping with these guiding principles.

Stella-Jones' products nevertheless remain a vital component of basic transportation and utility infrastructure and are integral to capital infrastructure projects that governments often initiate during times of economic slowdown. Such initiatives would drive demand, as they would potentially involve, in both maintenance and new installation endeavours, many of the Company's clients in the railway and electrical transmission and distribution industries.

In the absence of such government driven infrastructure projects, Management believes that sales will soften in the upcoming quarters until such time as general economic conditions improve. The Company's railway tie product category is the most susceptible to a prolonged economic downturn as its key customers in this category may reduce capital spending on special projects and track extensions as a result of lower traffic volumes.

In the short-term, Management remains focussed on cash generation and debt reduction, although the Company's long-term strategic vision, focused on continental expansion and consolidation, remains intact. Given the fragmented state of the wood treatment industry, acquisitions remain an integral part of the Company's growth plan. Management will continue to seek targets in its core railway tie and utility pole markets that meet its stringent investment requirements, provide synergistic opportunities and add value for Stella-Jones' shareholders.

August 12, 2009