



Stella-Jones Inc.

**Condensed Interim Consolidated
Financial Statements
(Unaudited)
March 31, 2023 and 2022**

Stella-Jones Inc.

Condensed Interim Consolidated Statements of Financial Position (Unaudited)

(expressed in millions of Canadian dollars)

	Note	As at March 31, 2023 \$	As at December 31, 2022 \$
Assets			
Current assets			
Accounts receivable		390	287
Inventories		1,376	1,238
Income taxes receivable		4	—
Other current assets		58	58
		<u>1,828</u>	<u>1,583</u>
Non-current assets			
Property, plant and equipment		781	755
Right-of-use assets		167	160
Intangible assets		169	171
Goodwill		376	369
Derivative financial instruments		24	29
Other non-current assets		6	6
		<u>3,351</u>	<u>3,073</u>
Liabilities and Shareholders' Equity			
Current liabilities			
Accounts payable and accrued liabilities		225	201
Income taxes payable		28	7
Current portion of long-term debt	4	103	1
Current portion of lease liabilities		41	41
Current portion of provisions and other long-term liabilities	5	11	9
		<u>408</u>	<u>259</u>
Non-current liabilities			
Long-term debt	4	1,054	940
Lease liabilities		134	126
Deferred income taxes		153	158
Provisions and other long-term liabilities	5	26	26
Employee future benefits		8	7
		<u>1,783</u>	<u>1,516</u>
Shareholders' equity			
Capital stock	6	192	194
Retained earnings		1,210	1,192
Accumulated other comprehensive income		166	171
		<u>1,568</u>	<u>1,557</u>
		<u>3,351</u>	<u>3,073</u>
Subsequent events	10		

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

Stella-Jones Inc.

Condensed Interim Consolidated Statements of Change in Shareholders' Equity

(Unaudited)

For the three-month periods ended March 31, 2023 and 2022

(expressed in millions of Canadian dollars)

	<u>Accumulated other comprehensive income</u>						Total shareholders' equity
	Capital stock	Retained earnings	Foreign currency translation adjustment	Translation of long-term debts designated as net investment hedges	Unrealized gains (losses) on cash flow hedges	Total	
	\$	\$	\$	\$	\$	\$	\$
Balance – January 1, 2023	194	1,192	261	(111)	21	171	1,557
Comprehensive income (loss)							
Net income	—	60	—	—	—	—	60
Other comprehensive loss	—	(1)	(1)	—	(4)	(5)	(6)
Comprehensive income (loss)	—	59	(1)	—	(4)	(5)	54
Dividends on common shares	—	(13)	—	—	—	—	(13)
Repurchase of common shares (note 6)	(2)	(28)	—	—	—	—	(30)
	(2)	(41)	—	—	—	—	(43)
Balance – March 31, 2023	192	1,210	260	(111)	17	166	1,568

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

Stella-Jones Inc.Condensed Interim Consolidated Statements of Change in Shareholders' Equity...*Continued*

(Unaudited)

For the three-month periods ended March 31, 2023 and 2022

(expressed in millions of Canadian dollars)

	Accumulated other comprehensive income						Total shareholders' equity
	Capital stock	Retained earnings	Foreign currency translation adjustment	Translation of long-term debts designated as net investment hedges	Unrealized gains on cash flow hedges	Total	
	\$	\$	\$	\$	\$	\$	\$
Balance – January 1, 2022	208	1,161	175	(98)	2	79	1,448
Comprehensive income (loss)							
Net income for the period	—	46	—	—	—	—	46
Other comprehensive income (loss)	—	4	(18)	4	9	(5)	(1)
Comprehensive income (loss) for the period	—	50	(18)	4	9	(5)	45
Dividends on common shares	—	(12)	—	—	—	—	(12)
Repurchase of common shares (note 6)	(3)	(37)	—	—	—	—	(40)
	(3)	(49)	—	—	—	—	(52)
Balance – March 31, 2022	205	1,162	157	(94)	11	74	1,441

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

Stella-Jones Inc.

Condensed Interim Consolidated Statements of Income

(Unaudited)

For the three-month periods ended March 31, 2023 and 2022

(expressed in millions of Canadian dollars, except earnings per common share)

	Note	2023	2022
		\$	\$
Sales		710	651
Expenses			
Cost of sales (including depreciation and amortization of \$21 (2022 - \$17))		574	551
Selling and administrative (including depreciation and amortization of \$4 (2022 - \$4))		41	33
		<u>615</u>	<u>584</u>
Operating income		<u>95</u>	<u>67</u>
Financial expenses		<u>14</u>	<u>6</u>
Income before income taxes		<u>81</u>	<u>61</u>
Income tax expense			
Current		24	13
Deferred		(3)	2
		<u>21</u>	<u>15</u>
Net income		<u>60</u>	<u>46</u>
Basic and diluted earnings per common share	6	<u>1.03</u>	<u>0.73</u>

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Stella-Jones Inc.

Condensed Interim Consolidated Statements of Comprehensive Income

(Unaudited)

For the three-month periods ended March 31, 2023 and 2022

(expressed in millions of Canadian dollars)

	2023	2022
	\$	\$
Net income	<u>60</u>	<u>46</u>
Other comprehensive income (loss)		
Items that may subsequently be reclassified to net income		
Losses on translation of financial statements of foreign operations	(1)	(18)
Gains on translation of long-term debt designated as hedges of net investment in foreign operations	—	4
Change in fair value of derivatives designated as cash flow hedges	(5)	13
Income tax on change in fair value of derivatives designated as cash flow hedges	1	(4)
Items that will not subsequently be reclassified to net income		
Remeasurements of post-retirement benefit obligations	(1)	5
Income taxes on remeasurements of post-retirement benefit obligations	<u>—</u>	<u>(1)</u>
	<u>(6)</u>	<u>(1)</u>
Comprehensive income	<u>54</u>	<u>45</u>

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

Stella-Jones Inc.

Condensed Interim Consolidated Statements of Cash Flows

(Unaudited)

For the three-month periods ended March 31, 2023 and 2022

(expressed in millions of Canadian dollars)

	Note	2023 \$	2022 \$
Cash flows from (used in)			
Operating activities			
Net income		60	46
Adjustments for			
Depreciation of property, plant and equipment		9	7
Depreciation of right-of-use assets		12	10
Amortization of intangible assets		4	4
Financial expenses		14	6
Income tax expense		21	15
Other		2	—
		<u>122</u>	<u>88</u>
Changes in non-cash working capital components			
Accounts receivable		(103)	(152)
Inventories		(138)	(60)
Other current assets		(2)	(7)
Accounts payable and accrued liabilities		11	12
		<u>(232)</u>	<u>(207)</u>
Interest paid		(15)	(8)
Income taxes paid		(7)	(9)
		<u>(132)</u>	<u>(136)</u>
Financing activities			
Net change in revolving credit facilities		217	239
Repayment of long-term debt		—	(32)
Repayment of lease liabilities		(11)	(10)
Repurchase of common shares	6	(30)	(39)
Other		(1)	—
		<u>175</u>	<u>158</u>
Investing activities			
Business combinations	3	(13)	—
Purchase of property, plant and equipment		(28)	(20)
Additions of intangible assets		(2)	(2)
		<u>(43)</u>	<u>(22)</u>
Net change in cash and cash equivalents during the period			
Cash and cash equivalents – Beginning of period			
Cash and cash equivalents – End of period			
		<u>—</u>	<u>—</u>
		<u>—</u>	<u>—</u>
		<u>—</u>	<u>—</u>

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

Stella-Jones Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

March 31, 2023 and 2022

1 Description of the business

Stella-Jones Inc. (with its subsidiaries, either individually or collectively, referred to as the “Company”) is North America’s leading producer of pressure-treated wood products. It supplies the continent’s major electrical utilities and telecommunication companies with wood utility poles and North America’s Class 1, short line and commercial railroad operators with railway ties and timbers. The Company also provides industrial products, which include wood for railway bridges and crossings, marine and foundation pilings, construction timbers and coal tar-based products. Additionally, the Company manufactures and distributes premium treated residential lumber and accessories to Canadian and American retailers for outdoor applications, with a significant portion of the business devoted to servicing Canadian customers through its national manufacturing and distribution network. The Company has treating and pole peeling facilities across Canada and the United States and sells its products primarily in these two countries. The Company’s headquarters are located at 3100 de la Côte-Vertu Blvd., in Saint-Laurent, Quebec, Canada. The Company is incorporated under the Canada Business Corporations Act, and its common shares are listed on the Toronto Stock Exchange (“TSX”) under the stock symbol SJ.

2 Significant accounting policies

Basis of presentation

The Company’s condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (“IFRS”) and Chartered Professional Accountants Canada Handbook Accounting - Part I, applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting.

These condensed interim consolidated financial statements were approved by the Board of Directors on May 9, 2023.

The same accounting policies, methods of computation and presentation have been followed in the preparation of these condensed interim consolidated financial statements as were applied in the annual consolidated financial statements for the year ended December 31, 2022.

These condensed interim consolidated financial statements should be read in conjunction with the Company’s annual consolidated financial statements for the year ended December 31, 2022, which have been prepared in accordance with IFRS.

Principles of consolidation

The condensed interim consolidated financial statements include the accounts of Stella-Jones Inc. and its controlled subsidiaries. Intercompany transactions and balances between these companies have been eliminated. All consolidated subsidiaries are wholly owned. The significant subsidiaries within the legal structure of the Company are as follows:

Subsidiary	Parent	Country of incorporation
Stella-Jones U.S. Holding Corporation	Stella-Jones Inc.	United States
Stella-Jones Corporation	Stella-Jones U.S. Holding Corporation	United States

Stella-Jones Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

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3 Business combination

On February 14, 2023, the Company acquired substantially all of the operating assets of IndusTREE Pole & Piling, LLC (“IndusTREE”). IndusTREE specialized in procuring, peeling and drying Southern Yellow Pine poles at its facility in Goodwater, Alabama and was acquired for synergistic reasons.

The total consideration for the acquisition was \$16 million (US\$13 million) and included a deferred consideration of one million dollars and the settlement of an advance payable by IndusTREE of two million dollars. Excluding acquisition-related costs of less than one million dollars recognized in the consolidated statement of income under selling and administrative expenses, the cash outlay was \$13 million (US\$ 10 million), financed through the Company’s existing credit facilities.

The following is a final summary of the assets acquired and the consideration transferred at fair value as at the acquisition date. The original transaction was made in U.S. dollars and converted into Canadian dollars as at the acquisition date.

(Amounts in millions of Canadian dollars)

Assets acquired	
Property, plant and equipment	8
Goodwill	8
	<hr/>
	16
Cash	13
Deferred consideration	1
Settlement of an advance payable by IndusTREE	2
	<hr/>
Consideration transferred	16

Goodwill is deductible for U.S. tax purposes and represents the future economic value associated with the acquired workforce and synergies with the Company’s operations. For impairment test purposes, goodwill is allocated to a CGU defined as plants specialized in the treatment of utility poles and residential lumber.

Stella-Jones Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

March 31, 2023 and 2022

4 Long-term debt

(Amounts in millions of Canadian dollars)	Year of maturity	As at March 31, 2023	As at December 31, 2022
Unsecured:			
Revolving credit facilities ^(a)	2026-2028	611	394
Term loan facilities			
US\$125, variable rate based on LIBOR or SOFR plus 1.725% ^(a)	2028	169	169
US\$100, fixed rates ranging from 3.27% to 4.47%, with quarterly amortization payments starting in 2026	2029-2030	135	135
US\$25, fixed rate of 4.52%	2029	34	34
Senior notes			
US\$75, fixed rate of 3.54%	2024	203	204
US\$75, fixed rate of 3.81%	2027		
Other		5	5
		1,157	941
Less: Current portion of long-term debt		103	1
		1,054	940

a) Unsecured Senior U.S. Farm Credit Facilities

On March 3, 2023, the Company amended and restated the U.S. Farm Credit Agreement in order to, among other things, (i) increase the amount available under the credit facilities from US\$350 million to US\$550 million, ii) extend the term of U.S. Farm Revolving Credit Facility in the amount of US\$150 million from April 29, 2026 to March 3, 2028, and iii) transition from London Interbank Offered Rate (“LIBOR”) references to Secured Overnight Financing Rate (“SOFR”). Revolving credit facility advances made prior to this amendment continued to apply LIBOR until the end of their term.

In order to maintain the credit facilities and senior notes in place, the Company needs to comply with customary affirmative covenants, negative covenants, reporting requirements and financial ratios. The Company is required to maintain a net funded debt-to-EBITDA ratio of no more than 3.50:1, an interest coverage ratio equal to or greater than 3.00:1 and a priority debt to equity ratio not more than 15%, which are measured on a quarterly basis. As at March 31, 2023, the Company was in full compliance with these covenants, requirements and ratios.

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Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

March 31, 2023 and 2022

5 Provisions and other long-term liabilities

(Amounts in millions of Canadian dollars)	As at March 31, 2023	As at December 31, 2022
Site remediation	17	18
Share-based payment plans	11	9
Others	9	8
	37	35
Less: Current portion of provisions and long-term liabilities	11	9
	26	26

The Company's share-based payment plans consist of cash-settled restricted stock unit, performance stock unit and deferred share unit plans.

Restricted stock units (RSUs) and Performance stock units (PSUs)

Under the Stock Unit Plan, RSUs and PSUs are granted to certain executives and key employees of the Company. RSUs and PSUs entitle the holders to receive a cash payment equal to the average closing price on the TSX of the Company's common shares for the five trading days preceding the vesting date multiplied by a factor which ranges from 0% to 200% based on the attainment of performance criteria and/or market conditions set out pursuant to the plan, provided the individual is still employed by the Company at time of vesting. RSUs vest ratably over a period of three years and PSUs are paid three years after the grant date.

Changes in outstanding RSUs for the three-month periods ended March 31, are as follows:

	2023	2022
RSUs outstanding - Beginning of period	122,315	103,963
Granted	65,479	88,763
Vested	(47,966)	(63,527)
Forfeited	—	(1,236)
RSUs outstanding - End of period	139,828	127,963

Changes in outstanding PSUs for the three-month periods ended March 31, are as follows:

	2023	2022
PSUs outstanding - Beginning of period	69,337	29,398
Granted	38,517	44,382
PSUs outstanding - End of period	107,854	73,780

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(Unaudited)

March 31, 2023 and 2022

Deferred share units (DSUs)

DSUs entitle non-executive directors of the Company to receive a minimum participation amount in the form of DSUs and they may elect to participate in the DSU plan for a portion of their Board fees. Such deferred remuneration is converted to DSUs based on the average closing price of the Company's common shares on the TSX of the five trading days immediately preceding the date such awards are granted to the non-employee director. DSUs are settled for cash only after a non-employee director ceases to act as a director.

Changes in outstanding DSUs for the three-month periods ended March 31, are as follows:

	2023	2022
DSUs outstanding - Beginning of period	44,333	20,131
Granted	—	1,246
DSUs outstanding - End of period	44,333	21,377

6 Capital stock and earnings per share

The following table provides the number of common shares outstanding for the three-month periods ended March 31:

	2023	2022
Number of common shares outstanding – Beginning of period	59,115,959	63,773,252
Common shares repurchased	(608,709)	(999,382)
Employee share purchase plans	5,988	8,198
Number of common shares outstanding – End of period	58,513,238	62,782,068

a) Capital stock

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares, issuable in series.

All issued shares are fully paid. The common shares provide for the right to receive notice of, attend and vote at all meetings of shareholders and receive dividends, subject to the prior rights of the preferred shares and any other shares ranking senior to the common shares. To date, the Company has not issued any preferred shares.

Stella-Jones Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

March 31, 2023 and 2022

b) Earnings per share

The following table provides the reconciliation, as at March 31, between basic earnings per common share and diluted earnings per common share:

(Amounts in millions of Canadian dollars, except per share amounts)	2023	2022
Net income applicable to common shares	\$60	\$46
Weighted average number of common shares outstanding*	58,801	63,272
Effect of dilutive stock options*	—	—
Weighted average number of diluted common shares outstanding*	58,801	63,272
Basic and diluted earnings per common share	\$1.03	\$0.73

* Number of shares is presented in thousands.

c) Normal Course Issuer Bid

On November 8, 2022, the TSX accepted the Company's Notice of Intention to Make a NCIB ("NCIB") to purchase for cancellation up to 5,000,000 common shares during the 12-month period commencing November 14, 2022 and ending November 13, 2023, representing approximately 9.6% of the public float of its common shares.

During the three-month period ended March 31, 2023, the Company repurchased for cancellation 608,709 common shares under its NCIB (March 31, 2022 - 999,382 common shares under the NCIB then in effect) for a total consideration of \$30 million (March 31, 2022 - \$40 million), representing an average price of \$49.27 per common share (March 31, 2022 - \$40.02). For the three-month period ended March 31, 2023, the Company's capital stock was reduced by two million dollars (March 31, 2022 - three million dollars) and the remaining \$28 million (March 31, 2022 - \$37 million) was accounted for as a decrease in retained earnings.

Stella-Jones Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

March 31, 2023 and 2022

7 Fair value measurement and financial instruments

The following table summarizes the Company's interest rate swap agreements:

(Amounts in millions of Canadian dollars)					As at March 31, 2023	As at December 31, 2022
Notional amount	Related debt instrument	Fixed rate %	Effective date	Maturity date	Notional equivalent CAS	Notional equivalent CAS
US\$50	Revolving credit facilities	0.796*	Dec. 2021	Dec. 2026	68	68
US\$125	Term loan facility	1.0769**	July 2021	June 2028	169	169

* Plus applicable margin based on pricing grid included in the revolving credit agreements.

** Plus set margin of 1.725%.

In March 2023, the Company amended its interest rate swap agreements and replaced its LIBOR interest derivatives used in cash flow hedging relationships with economically equivalent interest derivatives referencing SOFR. Prior to the transition from LIBOR to SOFR, the fixed swap rate was 0.872% and 1.125% plus applicable margin for the revolving credit facilities and the term loan facility, respectively.

The Company designates its interest rate swap agreements as cash flow hedges of the underlying debt. The cash flow hedge documentation allows the Company to substitute the underlying debt as long as the hedge effectiveness is demonstrated. As at March 31, 2023, all cash flow hedges were effective.

As at March 31, 2023, the fair value of interest swap agreements was \$24 million, recognized as non-current assets in the condensed interim consolidated statement of financial position (December 31, 2022 - \$29 million in the consolidated statement of financial position).

The fair value of these financial instruments has been estimated using the discounted future cash flow method and has been classified as Level 2 in the fair value hierarchy as per IFRS 7, *Financial Instruments: Disclosures*, as it is based mainly on observable market data, namely government bond yields and interest rates. A description of each level of the hierarchy is as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for these assets or liabilities, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: Inputs for the assets or liabilities that are not based on observable market data (unobservable inputs).

Financial instruments which are not measured at fair value on the statement of financial position are represented by accounts receivable, accounts payable and accrued liabilities and long-term debt. The fair values of accounts receivable and accounts payable and accrued liabilities approximate their carrying values due to their short-term nature. The long-term debt has a carrying value of \$1,157 million (December 31, 2022 - \$941 million) and a fair value of \$1,129 million (December 31, 2022 - \$908 million).

Stella-Jones Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

March 31, 2023 and 2022

8 Seasonality

The Company's operations follow a seasonal pattern, with utility poles, railway ties and industrial products shipments strongest in the second and third quarters to provide industrial end-users with product for their summer maintenance projects. Residential lumber sales follow the same seasonal pattern. Inventory levels of utility poles, railway ties and residential lumber are typically highest in the first quarter in advance of the summer shipping season.

9 Segment information

The Company operates within two business segments which are the production and sale of pressure-treated wood and the procurement and sales of logs and lumber.

The pressure-treated wood segment includes utility poles, railway ties, residential lumber and industrial products.

The logs and lumber segment comprises of the sales of logs harvested in the course of the Company's procurement process that are determined to be unsuitable for use as utility poles. Also included in this segment is the sale of excess lumber to local home-building markets. Assets and net income related to the logs and lumber segment are nominal.

Operating plants are located in six Canadian provinces and 18 American states. The Company also operates a large distribution network across North America.

Sales attributed to countries based on location of customer for the three-month periods ended March 31, are as follows:

(Amounts in millions of Canadian dollars)	2023	2022
Canada	138	177
U.S.	572	474
	710	651

Sales by product for the three-month periods ended March 31, are as follows:

(Amounts in millions of Canadian dollars)	2023	2022
Utility poles	362	254
Railway ties	195	175
Residential lumber	90	132
Industrial products	36	33
Pressure-treated wood	683	594
Logs and lumber	27	57
	710	651

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(Unaudited)

March 31, 2023 and 2022

Property, plant and equipment, right-of-use assets, intangible assets and goodwill attributed to the countries based on location are as follows:

(Amounts in millions of Canadian dollars)	As at March 31, 2023	As at December 31, 2022
Property, plant and equipment		
Canada	209	204
U.S.	572	551
	781	755
Right-of-use assets		
Canada	22	22
U.S.	145	138
	167	160
Intangible assets		
Canada	54	54
U.S.	115	117
	169	171
Goodwill		
Canada	21	21
U.S.	355	348
	376	369

10 Subsequent events

On May 9, 2023, the Board of Directors declared a quarterly dividend of \$0.23 per common share payable on June 23, 2023 to shareholders of record at the close of business on June 5, 2023.