



November 30, 2006

Paper & Forest Products

Stock Rating:
Sector Performer

Sector Weighting:
Underweight

12-18 mo. Price Target \$40.00
WFT-TSX (11/29/06) \$39.42

Key Indices: None

3-5-Yr. EPS Gr. Rate (E)	NM
52-week Range	\$34.85-\$44.00
Shares Outstanding	42.8M
Float	22.5M Shrs
Avg. Daily Trading Vol.	NM
Market Capitalization	\$1,685.8M
Dividend/Div Yield	\$0.56 / 1.4%
Fiscal Year Ends	December
Book Value	\$45.60 per Shr
2006 ROE (E)	1.0%
LT Debt	\$614.2M
Preferred	Nil
Common Equity	\$1,950.3M
Convertible Available	Yes

Earnings per Share	Prev	Current
2005		\$1.90A
2006		\$0.63E
2007	\$1.25E	\$1.14E

P/E		
2005		20.7x
2006		62.6x
2007	31.5x	34.6x

EBITDA (\$ mlns.)	
2005	\$455.2
2006E	\$380.2
2007E	\$363.0

Company Description

West Fraser is one of Canada's largest integrated forest products companies with plants in B.C. and Alberta producing solid wood, pulp, newsprint, linerboard and kraft paper.

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West Fraser Timber Co. Ltd.

Acquisition of IP Sawmills A Good Strategic Move At A Reasonable Price

- West Fraser announced on November 29 that it has entered into an agreement to acquire 13 sawmills from IP (IP-SO) for approximately US\$325 million. The deal is expected to be dilutive to EBITDA over the next 1-2 years, but we still think it is a good move at a reasonable price.
- The deal is fully funded through cash on hand and available credit facilities. No equity will be issued, and on a pro forma basis WFT's net debt/capital ratio will remain low at 26%. We think the actual synergies will be in the US\$35-45 million range, as opposed to the US\$23 million stated by mgmt.
- We estimate that the price represents 5.9x normalized EBITDA before synergies, and 4.2x after the US\$23 million in synergies quoted by mgmt. The TEV/2005 EBITDA multiple is 2.8x, vs. 4.7x for Interfor, 4.9x for West Fraser and 8.2x for Canfor. However, it is EBITDA negative in 2006/H2.
- We are reducing our 2007E EPS estimate from \$1.25 to \$1.14. We like the transaction from a strategic and long-term value perspective, but we are reducing our target from \$42 to \$40 to reflect the short-term pressure on earnings. We think lumber prices will remain low through mid-2008.

Stock Price Performance



Source: Reuters

All figures in Canadian dollars, unless otherwise stated.

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See "Price Target Calculation" and "Key Risks to Price Target" sections at the end of this report, where applicable.

The acquisition price of US\$325 million, including roughly US\$65 million in working capital, is subject to certain post-closing adjustments. The transaction, which is also subject to U.S. regulatory approvals and customary conditions, is expected to close in the first quarter of 2007.

The purchase price is lower than expected, but reflects the losses expected to be realized in the short term. West Fraser is paying US\$181/mfbm of lumber capacity, while precedent transactions have been done at an average of US\$200/mfbm. We estimate that the price represents 5.9 times normalized EBITDA before synergies and 4.2 times after the US\$23 million in synergies suggested by management. As indicated in Exhibit 1, the IP assets are being acquired at a significantly lower TEV/2005 EBITDA multiple than what the "average" Canadian lumber producer is currently trading (i.e., 2.8x vs. 5.9x).

In our view, we think West Fraser will be able to improve the EBITDA of the acquired mills by US\$35-45 million over the next 3 years without spending additional capital. This range is consistent with an "execution gap" of US\$20-\$25/mfb that is typical in many sawmills in the region. Note that West Fraser significantly exceeded the synergy target associated with its previous acquisition of Weldwood. Having said that, we are sticking with WFT's stated target of US\$23 million for the time being.

Exhibit 1. Valuation Before Synergies

	TEV/EBITDA	
	2004	2005
Canfor	3.6	8.2
West Fraser	5.6	4.9
Interfor	4.5	4.7
Average	4.6	5.9
IP Sawmills Price	2.9	2.8

Source: Company reports and CIBC World Markets Inc.

Based on benchmarking surveys, the acquired mills are on average more profitable than other mills in the region. West Fraser has indicated that the majority of the units are in the first two quartiles on the region's cost curve. However, with the price of Southern Yellow Pine lumber hovering near its 10-year low, the mills as a group were EBITDA negative in the third quarter. Although we think lumber prices are currently unsustainably low, we expect the results will be even worse in Q4/06.

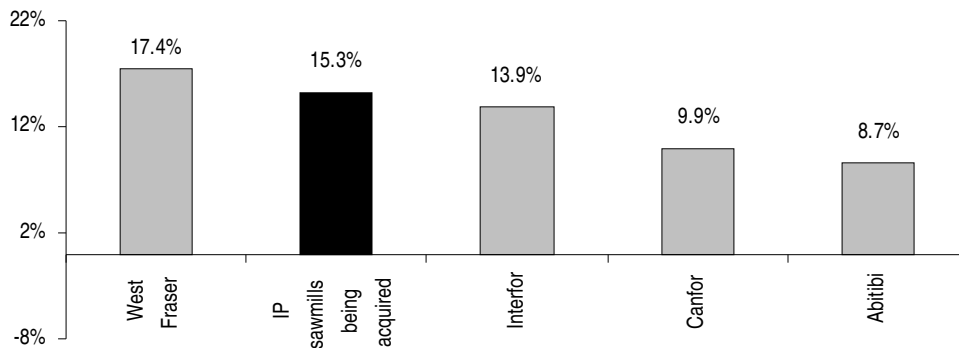
(Note that the price spread between Western SPF lumber and Southern Yellow Pine lumber has been very volatile in recent years. For modeling purposes, management has suggested that, on a normalized basis, a US\$40 premium be applied to the Southern Yellow Pine.)

Exhibit 2. Sawmills

State	Location	Mill Type	2005 Production
Sawmills (MMfbm)			
Alabama	Citronelle	Dimension	84
Alabama	Maplesville	Dimension	107
Alabama	Opelika	Dimension	95
Arkansas	Leola	Dimension	179
Florida	McDavid	Dimension	211
Florida	Whitehouse	Dimension	96
Georgia	Augusta	Dimension	144
Georgia	Folkston	Dimension	97
North Carolina	Riegelwood	Dimension	199
North Carolina	Seaboard	Dimension	100
South Carolina	Newberry	Stud	140
Texas	Henderson	Dimension	142
Texas	New Boston	Dimension	160
Total Sawmills			1,754

Source: Company reports and CIBC World Markets Inc.

Exhibit 3. 2005 Lumber EBITDA Margins



Source: Company reports and CIBC World Markets Inc.

Upon completion of the transaction, West Fraser will be the second largest lumber producer in North America with combined Canadian and U.S. production capacity of approximately 6.2 billion board feet. The deal increases WFT’s lumber capacity by approximately 1.8 BBF, or roughly 40%. (West Fraser already owns two sawmills in the U.S. located in Huttig, Arkansas and Joyce, Louisiana, which have a combined annual production capacity of 420 million board feet.)

Management has indicated that it does not plan to close any of the IP sawmills. However, we would be surprised if 4-5 of the mills (i.e., those with 100 mmfbm of capacity or less) were not closed during the ongoing correction in prices.

The bottom-line is that we think this acquisition provides WFT with meaningful growth at a reasonable price. However, this is also a good strategic move for a number of reasons.

- The deal positions WFT to “grow around” its exposure to the Mountain Pine Beetle problem in Western Canada. Specifically, after another 7-10 years of accelerated salvage harvest in the B.C. Interior, we expect West Fraser’s allowable annual cut to decrease by as much as 50%. Even in the interim period, West Fraser is experiencing lower productivity and less profitable grade mixes as a result of the dead “beetle wood” being dryer than expected.
- The wood basket in the U.S. South is among the lowest cost in North America, and is steadily growing. With this deal, the share of WFT’s sawmilling capacity located in the U.S. south rises from 10% to 36%.
- The southern U.S. is also North America’s fastest growing market for wood products, and routinely accounts for roughly 40% of all housing starts on the continent. As a result, the new sawmills will enjoy a distinct freight advantage over WFT’s other operations – an advantage we think will increase over time.
- By growing in the U.S., West Fraser gets roughly 1/3 of its production behind U.S. trade barriers.
- West Fraser becomes more naturally hedged against shifts in the C\$/US\$ exchange rate by virtue of its larger operations in the U.S.

Price Target Calculation

Our 12- to 18-month price target of \$40.00 is based on a multiple of 6.0x of our new 2007 EBITDA estimate of \$363 million plus the expected free cash flow of \$73 million over the next 12 months, the remaining synergies of \$17 million and the expected duty refund of \$292 million. The forecast TEV of \$2.6 billion is reduced by the current proforma net debt of \$956 billion, resulting in an equity value of \$1.7 billion. The Canadian paper & forest products stocks have traded at an average TEV/EBITDA multiple of 5.0x. However, we think this average multiple is too low, as it reflects the depressed industry conditions of the last five years rather than a full cycle. Our calculation suggests that a multiple of 6.0x on West Fraser would provide investors with a reasonable return over a cycle.

Key Risks To Price Target

Potential risks to our price target include a weaker-than-expected global economy, which would undermine pulp from moving higher, a longer and deeper correction in U.S. housing starts than expected which would hurt lumber prices, and volatility in the Canadian/U.S. exchange rate.

Exhibit 4. Income Statement (\$ mlns., except per share)

	2005A	2006E	2007E
Sales	\$3,576.7	\$3,380.1	\$3,937.4
Cost of Sales	\$3,121.5	\$2,999.9	\$3,574.3
EBITDA	\$455.2	\$380.2	\$363.0
Depreciation	\$255.4	\$244.8	\$262.6
Operating Profit	\$199.9	\$135.4	\$100.5
Other Expenses (Gains)	\$0.0	\$0.0	\$0.0
Financial Expenses	\$48.4	\$40.7	\$27.0
Earnings Before Income Taxes	\$151.4	\$94.7	\$73.5
Income Taxes	\$42.3	(\$11.5)	\$24.2
Net Earnings	\$109.1	\$106.2	\$49.2
Net Earnings Per Share	\$2.49	\$2.46	\$1.14
EPS Before Unusual Items	\$1.90	\$0.63	\$1.14

Source: Company reports and CIBC World Markets Inc.

Our EPS estimates are shown below:

	1 Qtr.	2 Qtr.	3 Qtr.	4 Qtr.	Yearly
2005 Current	\$0.99A	\$1.03A	(\$0.23A)	\$0.11A	\$1.90A
2006 Current	\$0.76A	(\$0.05A)	(\$0.18A)	\$0.10E	\$0.63E
2007 Prior	--	--	--	--	\$1.25E
2007 Current	--	--	--	--	\$1.14E

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Canfor Corporation (CFP-TSX, \$10.02, Sector Underperformer)

International Forest Products Limited (2g, 12) (IFP.A-TSX, \$7.10, Sector Outperformer)

International Paper Co. (2g) (IP-NYSE, US\$32.55, Sector Outperformer)

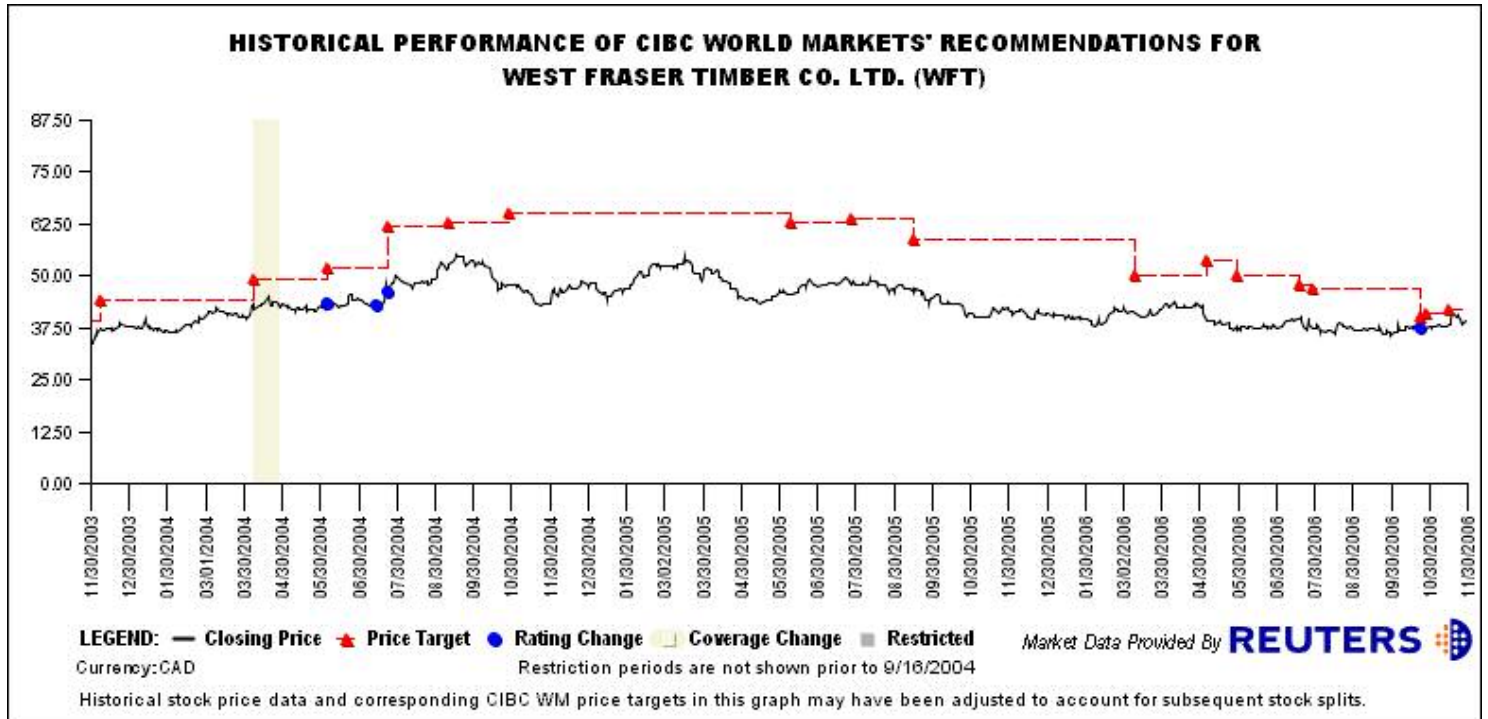
West Fraser Timber Co. Ltd. (2g) (WFT-TSX, \$39.42, Sector Performer)

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CIBC World Markets Price Chart



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Date	Change Type	Closing Price	Rating	Price Target	Coverage
12/08/2003	▲	37.25	SP	44.00	Don Roberts
04/07/2004	▲ █	43.45	SP	49.00	Herve Carreau, CFA
04/28/2004	█	42.50	SP	49.00	Don Roberts
06/04/2004	▲ ●	43.44	SO	52.00	Don Roberts
07/14/2004	●	43.00	SP	52.00	Don Roberts
07/23/2004	▲ ●	46.00	SO	62.00	Don Roberts
09/08/2004	▲	51.70	SO	63.00	Don Roberts
10/27/2004	▲	47.92	SO	65.00	Don Roberts
06/07/2005	▲	45.51	SO	63.00	Don Roberts
07/26/2005	▲	48.00	SO	64.00	Don Roberts
09/14/2005	▲	46.81	SO	59.00	Don Roberts
03/09/2006	▲	41.18	SO	50.00	Don Roberts
05/04/2006	▲	40.09	SO	54.00	Don Roberts
05/29/2006	▲	37.79	SO	50.00	Don Roberts
07/18/2006	▲	39.84	SO	48.00	Don Roberts
07/28/2006	▲	37.50	SO	47.00	Don Roberts
10/22/2006	▲ ●	37.43	SP	40.00	Don Roberts
10/26/2006	▲	37.40	SP	41.00	Don Roberts
11/13/2006	▲	37.70	SP	42.00	Don Roberts

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SO	Sector Outperformer	Stock is expected to outperform the sector during the next 12-18 months.
SP	Sector Performer	Stock is expected to perform in line with the sector during the next 12-18 months.
SU	Sector Underperformer	Stock is expected to underperform the sector during the next 12-18 months.
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R	Restricted	CIBC World Markets is restricted*** from rating the stock.
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O	Overweight	Sector is expected to outperform the broader market averages.
M	Market Weight	Sector is expected to equal the performance of the broader market averages.
U	Underweight	Sector is expected to underperform the broader market averages.
NA	None	Sector rating is not applicable.

**Broader market averages refer to the S&P 500 in the U.S. and the S&P/TSX Composite in Canada.

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Sector Outperformer (Buy)	325	39.2%	Sector Outperformer (Buy)	168	51.7%
Sector Performer (Hold/Neutral)	401	48.4%	Sector Performer (Hold/Neutral)	194	48.4%
Sector Underperformer (Sell)	72	8.7%	Sector Underperformer (Sell)	33	45.8%
Restricted	18	2.2%	Restricted	16	88.9%

Ratings Distribution: Paper & Forest Products Coverage Universe

(as of 29 Nov 2006)	Count	Percent	Inv. Banking Relationships	Count	Percent
Sector Outperformer (Buy)	3	18.8%	Sector Outperformer (Buy)	3	100.0%
Sector Performer (Hold/Neutral)	8	50.0%	Sector Performer (Hold/Neutral)	6	75.0%
Sector Underperformer (Sell)	5	31.3%	Sector Underperformer (Sell)	4	80.0%
Restricted	0	0.0%	Restricted	0	0.0%

Paper & Forest Products Sector includes the following tickers: A, BOW, CAS, CFP, CFX.UN, CTL, DTC, FPS, IFP.A, IP, LPX, MERC, NBD, TBC, WFT, WY.

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