Catalyst Paper Corporation is a leading producer of mechanical printing papers in North America, headquartered in Richmond, British Columbia. The company also produces market kraft pulp and owns Western Canada’s largest paper recycling facility. With five mills employing approximately 3,000 people at sites within a 160-kilometre radius on the south coast of BC, Catalyst has a combined annual capacity of 2.4 million tonnes of product. Catalyst’s common shares trade on the Toronto Stock Exchange under the symbol CTL.
taking the initiative

2007 was a year in which Catalyst took the initiative – both to address its cost structure in the short term, and to secure a strategically differentiated marketplace position in the longer term.

### Financials

(In millions of dollars, except where otherwise stated)

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$1,714.6</td>
<td>$1,882.5</td>
<td>$1,823.9</td>
</tr>
<tr>
<td>EBITDA</td>
<td>27.0</td>
<td>211.0</td>
<td>155.2</td>
</tr>
<tr>
<td>EBITDA before specific items</td>
<td>116.7</td>
<td>211.0</td>
<td>161.9</td>
</tr>
<tr>
<td>Operating earnings (loss)</td>
<td>(149.4)</td>
<td>3.9</td>
<td>(25.1)</td>
</tr>
<tr>
<td>Net earnings (loss)</td>
<td>(31.6)</td>
<td>15.9</td>
<td>(25.6)</td>
</tr>
<tr>
<td>Net earnings (loss) before specific items</td>
<td>(89.3)</td>
<td>(25.0)</td>
<td>(64.6)</td>
</tr>
<tr>
<td>Cash flows provided by operations</td>
<td>(2.7)</td>
<td>127.2</td>
<td>60.7</td>
</tr>
<tr>
<td>Total debt</td>
<td>785.8</td>
<td>860.5</td>
<td>867.3</td>
</tr>
<tr>
<td>Total assets</td>
<td>2,453.4</td>
<td>2,637.7</td>
<td>2,695.9</td>
</tr>
<tr>
<td>Capital expenditures</td>
<td>85.8</td>
<td>93.2</td>
<td>95.2</td>
</tr>
<tr>
<td>Performance improvements</td>
<td>81.2</td>
<td>74.0</td>
<td>84.0</td>
</tr>
<tr>
<td>Average spot foreign exchange rate US$/C$</td>
<td>0.930</td>
<td>0.882</td>
<td>0.825</td>
</tr>
<tr>
<td>Period-end spot foreign exchange rate US$/C$</td>
<td>1.012</td>
<td>0.858</td>
<td>0.858</td>
</tr>
</tbody>
</table>

1. EBITDA, EBITDA before specific items, and net earnings (loss) before specific items are non-GAAP measures. Refer to section 9, “Non-GAAP measures” for further details.
2. Total debt comprises long-term debt, including current portion.
3. Average spot foreign exchange rate is the average Bank of Canada noon spot rate over the reporting period.
4. Period-end spot foreign exchange rate is the Bank of Canada noon spot rate.
5. Thousands of tonnes.
6. Number of medical incidents per 200,000 hours worked.
7. Number of lost-time injuries per 200,000 hours worked.
8. Employee figures for 2006-2007 are as of January 1 (2007 and 2008, respectively) to account for acquisition and restructuring impacts.
9. Thousands of tonnes CO₂e/year.

### Production capacity

- Speciality Paper 47%
- Pulp 28%
- Newsprint 25%

### 2007 geographic sales distribution

- United States 50%
- Asia and Australasia 21%
- Canada 12%
- Latin America 9%
- Europe and Other 8%
PRESIDENT’S MESSAGE

to our shareholders

Catalyst Paper achieved significant performance improvements in 2007, but gains were outweighed by the negative impacts of escalating currency appreciation, fibre cost increases, the coastal fibre strike and other challenging business conditions. As a result, we ended the year with an operating loss.

We took decisive steps in 2007 to reduce our cost structure and improve our grade profitability; even so we ended the year with a net loss of $31.6 million, or $0.15 per common share, on sales of $1,714.6 million. This compares with a net loss in 2006 of $15.9 million, or $0.07 per common share, on sales of $1,882.5 million.

Operating loss in 2007 was $149.4 million, compared with operating earnings of $3.9 million in 2006. The decline in earnings was primarily due to higher fibre costs, weaker paper prices, and stronger Canadian currency; as well as reflecting one-time restructuring costs which are expected to substantially lower future manufacturing expenses. These combined factors resulted in earnings before interest, taxes, depreciation and amortization (EBITDA) of $27 million in 2007, down from $211 million in 2006.

The business climate

Rising input costs, especially for virgin fibre, were one of four major business challenges in 2007. First, sawmill production was curtailed as a result of a 13-week strike in the British Columbia coastal forest industry, causing both a drop in availability and an increase in prices. The strike forced production curtailments of nearly 161,000 tonnes and reduced EBITDA by some $25 million.

Second, fibre costs were $78 million higher than in 2006 due to tight supply, adverse weather conditions, fuel surcharges and sawmill production curtailment.

Third, our results were affected by the strong appreciation of the Canadian dollar as it reached levels, relative to the U.S. dollar, that have not been seen in more than half a century.

Our fourth major challenge in 2007 was weak market conditions for paper. This netted to lower transaction prices for all our grades except directory, even though pricing gained momentum late in the year. The general weakness of paper markets was only partly balanced by the continuing strength of the pulp markets.

Tightening supply for coated grades supported price increases in the latter part of 2007, but still left average prices for the year below 2006 levels. Demand for uncoated grades was on balance flat, with soft pricing through most of the year. Directory demand was steady and average prices were up. Declining newsprint consumption in the U.S. market drove prices down, although announced capacity closures and west coast production curtailments supported our price increase announcements of $85 per tonne since November 2007.

Taking the initiative

Once again people throughout Catalyst delivered on a range of cost reduction and performance improvements in 2007 that resulted in $81 million in year-over-year realized improvements.

During 2007, we implemented a broad restructuring which reduced our total employment by 15 per cent, or more than 550 positions, and brought workforce levels closer to competitive benchmarks in the industry. We also moved our head office and consolidated certain mill support functions to achieve cost savings and efficiencies.

All of these initiatives were completed by year-end and while they resulted in restructuring costs of $58.3 million in 2007, related mainly to severance, we expect to realize annualized savings of approximately $67 million going forward.

Beyond workforce-related improvements, savings were achieved through product and customer optimization and in chemical and energy costs.
We continued during 2007 to strengthen our position as a preferred supplier of specialty mechanical grades and optimized production of higher gloss and super-bright lines with the potential for improved margins and stronger customer relationships.

Grade and product-optimization contributed $21 million in EBITDA improvement in 2007. We also introduced our Catalyst Cooled paper which is manufactured with no net increase of carbon emissions to the atmosphere. This initiative places us at the forefront of manufacturing-sector efforts to translate environmental performance into clear marketplace differentiation.

**Capital expenditures**

We concluded in 2007 a five-year period of significant capital expenditures, largely to enable a shift to higher-margin products while at the same time reducing unit costs and improving environmental performance.

Total capital expenditures were $85.8 million in 2007 with spending largely focused on high-return projects that provide product-quality benefits. 2008 capital spending is expected to return to a maintenance-of-business level in the range of $35 million.

**Outlook for 2008**

In mid-February 2008, we were pleased to make two announcements with a significant bearing on the current outlook. The first was a definitive agreement (subject to various customary conditions) to acquire a low-cost recycled newsprint mill in Arizona – the first expansion of Catalyst’s manufacturing base beyond Canada. The second was a $12 million capital upgrade at Port Alberni which, combined with a landmark labour agreement with union locals, enables the restart of the No. 4 directory paper machine indefinitely idled since September 1, 2007. This will return the mill to a two-machine operation with a significantly improved cost structure.

We anticipate that 2008 will remain a challenging year for the forest products sector. Early indications are that U.S. economic contraction could affect demand; however capacity rationalization is expected to cushion the impact on our sector. On the input side, we expect constraints on fibre supply to continue as sawmills adjust to weak housing markets. While our long-term wood fibre contracts and internal recycle capacity allow reasonable security of furnish, additional fibre-related production curtailments are likely.

Safety is a key performance metric at Catalyst. Results in 2007 were disappointing and we will sharpen our focus on safety in all work practices across our mills in 2008.

The coming year also promises to be a pivotal one for climate change-related regulatory efforts at various levels of government and in mid-February, the British Columbia government announced a carbon tax to take effect July 1, 2008, subject to approval by the legislature. The tax will apply to virtually all fossil fuels, including gasoline, diesel, natural gas, coal, propane, and home heating fuel – making it among the broadest and most comprehensive in the world. With operational expertise in emissions tracking, reporting, and early action on carbon reductions, Catalyst is prepared to address emerging requirements and potential business risks and opportunities.

Finally, the cost and performance discipline that we demonstrated in 2007 will continue to be our core strengths in 2008. We will also remain focused on social and environmental indicators and performance as a key means of supporting improved financial results.

Richard Garneau
President and Chief Executive Officer
February 13, 2008