



KRUGER PRODUCTS L.P.

**UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENT
FOR THE 3-MONTH PERIODS ENDED APRIL 1, 2018 AND MARCH 26, 2017**

Kruger Products L.P.

Unaudited Condensed Consolidated Statement of Financial Position

(tabular amounts are in thousands of Canadian dollars)

	April 1, 2018	December 31, 2017
	\$	\$
Assets		
Current assets		
Cash and cash equivalents (note 14)	10,477	8,837
Trade and other receivables	137,724	113,194
Receivables from related parties (note 11)	54	85
Current portion of advances to partners (note 9)	6,008	1,928
Inventories	210,728	192,394
Income tax recoverable	333	522
Prepaid expenses	15,597	8,007
	<u>380,921</u>	<u>324,967</u>
Non-current assets		
Advances to partners (note 9)	-	4,489
Property, plant and equipment (note 6)	768,289	761,610
Other long-term assets	-	6,331
Goodwill	160,939	160,939
Intangible assets	15,032	15,327
Deferred income taxes	28,387	26,092
	<u>1,353,568</u>	<u>1,299,755</u>
Total assets		
Liabilities		
Current liabilities		
Bank indebtedness (note 14)	9,140	9,051
Trade and other payables	194,087	190,698
Payables to related parties (note 11)	8,287	2,596
Income tax payable	729	498
Distributions payable (notes 9 and 11)	10,447	10,382
Current portion of provisions (note 8)	280	333
Current portion of long-term debt (note 13)	198,204	190,947
	<u>421,174</u>	<u>404,505</u>
Non-current liabilities		
Long-term debt (note 13)	262,316	225,368
Provisions (note 8)	6,086	5,973
Pensions (note 7)	103,285	119,558
Post-retirement benefits (note 7)	60,100	60,457
	<u>852,961</u>	<u>815,861</u>
Liabilities to non-unitholders		
Current portion of Partnership units liability (note 9)	1,928	1,928
Long-term portion of Partnership units liability (note 9)	159,131	158,381
	<u>161,059</u>	<u>160,309</u>
Total Partnership units liability		
	<u>1,014,020</u>	<u>976,170</u>
Total liabilities		
Equity		
Partnership units (note 9)	361,300	356,240
Deficit	(97,683)	(99,742)
Accumulated other comprehensive income	75,931	67,087
	<u>339,548</u>	<u>323,585</u>
Total equity	<u>339,548</u>	<u>323,585</u>
Total equity and liabilities	<u>1,353,568</u>	<u>1,299,755</u>
Subsequent events (notes 9 and 16)		

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

Kruger Products L.P.
Unaudited Condensed Consolidated Statement of Comprehensive Income

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars)

	3-month period ended April 1, 2018 \$	3-month period ended March 26, 2017 \$
Revenue (note 11)	323,735	289,271
Expenses		
Cost of sales (note 11)	287,369	244,254
Selling, general and administrative expenses (note 11)	22,953	23,221
(Gain) loss on sale of non-financial assets	(215)	13
Restructuring costs, net (note 8)	-	11
Operating income	<u>13,628</u>	<u>21,772</u>
Interest expense	11,313	10,264
Other expense (note 5)	<u>1,788</u>	<u>1,945</u>
Income before income taxes	527	9,563
Income taxes (note 10)	<u>(1,050)</u>	<u>2,614</u>
Net income for the period	<u>1,577</u>	<u>6,949</u>
Other comprehensive income		
Items that will not be reclassified to net income:		
Remeasurements of pensions	16,806	(2,567)
Remeasurements of post-retirement benefits	638	(884)
Items that may be subsequently reclassified to net income:		
Cumulative translation adjustment	<u>8,844</u>	<u>(765)</u>
Total other comprehensive income (loss) for the period	<u>26,288</u>	<u>(4,216)</u>
Comprehensive income for the period	<u><u>27,865</u></u>	<u><u>2,733</u></u>

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

Kruger Products L.P.

Unaudited Condensed Consolidated Statement of Changes in Equity

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

	Partnership units		Deficit \$	Accumulated other comprehensive income \$	Total equity \$
	#	\$			
As of January 1, 2017	56,376,788	336,576	(42,792)	88,849	382,633
Distributions payable (note 9)	-	-	(10,203)	-	(10,203)
Fair value adjustment (note 9)	-	115	(115)	-	-
Change in actuarial loss on pension	-	-	(2,567)	-	(2,567)
Change in actuarial loss on post-retirement benefits	-	-	(884)	-	(884)
Cumulative translation adjustment	-	-	-	(765)	(765)
Net income for the period	-	-	6,949	-	6,949
Issuance of partnership units (note 9)	309,196	4,715	-	-	4,715
As of March 26, 2017	56,685,984	341,406	(49,612)	88,084	379,878
As of January 1, 2018	57,675,039	356,240	(99,742)	67,087	323,585
Change in accounting policy (note 3(i))	-	-	(6,331)	-	(6,331)
Restated total equity as of January 1, 2018	57,675,039	356,240	(106,073)	67,087	317,254
Distributions payable (note 9)	-	-	(10,447)	-	(10,447)
Fair value adjustment (note 9)	-	184	(184)	-	-
Change in actuarial gain on pension	-	-	16,806	-	16,806
Change in actuarial gain on post-retirement benefits	-	-	638	-	638
Cumulative translation adjustment	-	-	-	8,844	8,844
Net income for the period	-	-	1,577	-	1,577
Issuance of partnership units (note 9)	361,174	4,876	-	-	4,876
As of April 1, 2018	58,036,213	361,300	(97,683)	75,931	339,548

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

Kruger Products L.P.

Unaudited Condensed Consolidated Statement of Cash Flows

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars)

	3-month period ended April 1, 2018 \$	3-month period ended March 26, 2017 \$
Cash flows from (used in) operating activities		
Net income for the period	1,577	6,949
Items not affecting cash		
Depreciation	12,815	11,748
Amortization	295	240
Loss (gain) on sale of property, plant and equipment	434	(2)
Change in amortized cost of Partnership units liability (note 5)	2,678	2,529
Foreign exchange gain (note 5)	(241)	(584)
Change in fair value of derivatives (note 5)	(649)	-
Interest expense	11,313	10,264
Pension and post-retirement benefits (note 7)	3,344	2,513
Provisions (note 8)	48	244
Income taxes	(1,050)	2,614
Loss (gain) on sale of non-financial assets	(215)	13
Total items not affecting cash	28,772	29,579
Net change in non-cash working capital (note 15)	(36,621)	(28,860)
Contributions to pension and post-retirement benefit plans	(3,987)	(3,738)
Provisions paid (note 8)	(41)	(334)
Income tax payments	(352)	(1,507)
Net cash from (used in) operating activities	(10,652)	2,089
Cash flows from (used in) investing activities		
Purchases of property, plant and equipment	(15,718)	(12,734)
Capitalized interest paid	-	(222)
Government assistance received	-	916
Proceeds on sale of property, plant and equipment	331	1,043
Net cash used in investing activities	(15,387)	(10,997)
Cash flows from (used in) financing activities		
Proceeds from long-term debt	38,050	28,015
Repayment of long-term debt	(285)	(126)
Payment of deferred financing fees	(232)	(9)
Interest paid on long-term debt	(3,240)	(2,558)
Distributions and advances paid, net (note 9)	(7,025)	(9,018)
Net cash from financing activities	27,268	16,304
Effect of exchange rate changes on cash and cash equivalents held in foreign currency	322	(56)
Increase in cash and cash equivalents during the period	1,551	7,340
Cash and cash equivalents - Beginning of period (note 14)	(214)	27,504
Cash and cash equivalents - End of period (note 14)	1,337	34,844

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

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

1 General information

Kruger Products L.P. (KPLP or the Partnership) is a limited partnership registered in the Province of Quebec, Canada whose partners are Kruger Inc. (ultimate parent), KPGP Inc. (KPGP), and KP Tissue Inc. (KPT). The Partnership manufactures, sells and distributes tissue products for household, industrial and commercial use. The Partnership has plants in New Westminster, British Columbia; Crabtree, Quebec; Sherbrooke, Quebec; Gatineau, Quebec; Scarborough and Trenton, Ontario and Memphis, Tennessee. The Partnership's headquarters are located in Mississauga, Ontario, Canada.

2 Basis of presentation

These unaudited condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) applicable to the preparation of interim financial statements, including International Accounting Standard (IAS) 34 - Interim Financial Reporting as issued by the International Accounting Standards Board (IASB), and with interpretations of the International Financial Reporting Committee which the Canadian Accounting Standards Board has approved for incorporation into Part 1 of the CPA Canada Handbook - Accounting. These unaudited condensed consolidated financial statements should be read in conjunction with the annual consolidated financial statements of the Partnership for the year ended December 31, 2017.

The 3-month period ended April 1, 2018 represents the 91 day period from January 1 to April 1, 2018 and the 3-month period ended March 26, 2017 represents the 85 day period from January 1 to March 26, 2017.

These unaudited condensed consolidated financial statements were approved by the board of directors of KPGP on May 9, 2018.

3 Summary of significant accounting policies

The significant accounting policies that have been used in the preparation of these unaudited condensed consolidated financial statements are described in the annual consolidated financial statements of the Partnership for the year ended December 31, 2017 and have been applied to all periods presented except the following accounting policies, which were adopted effective January 1, 2018.

- (i) IFRS 15, Revenue from Contracts with Customers, specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with some informative, relevant disclosures. The Partnership adopted the standard on January 1, 2018 using the modified retrospective approach. The adoption of this standard had no significant impact on the unaudited condensed consolidated financial statements. The application of IFRS 15 resulted in a change in the revenue recognition related to dispensers and related revenue. A transitional adjustment of \$6.3 million, to reduce the balance related to the dispensers recorded in Other long term assets at December 31, 2017, was recognized in the deficit on the date of initial application, January 1, 2018. Refer to the unaudited condensed consolidated statement of changes in equity for the restated total equity as of January 1, 2018.

The Partnership recognizes revenue when control of the products has transferred, being when the products are delivered to, and accepted by, the customer (based on shipping terms).

Revenue is measured based on the price specified in the sales contract and is net of discounts, rebates and allowances. Reductions to revenue for expected and actual payments to customers for rebates and allowances are based on actual expenses incurred during the period, on estimates of what is due to customers for estimated credits earned during the period and any adjustments for credits based on actual activity. Revenue is only recognized to the extent that it is highly probable that a significant reversal will not occur. A contract liability is recognized for expected discounts, rebates and allowances payable to customers in relation to sales made in the reporting period. The contract liability is included in trade and other payables.

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Notes to Unaudited Condensed Consolidated Financial Statements

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

- (ii) IFRS 9, Financial Instruments. In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments, bringing together the classification and measurement, impairment and hedge accounting phases of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement. The adoption of this standard had no significant impact on the unaudited condensed consolidated financial statements.

(i) Investments and other financial assets

Classification

Beginning January 1, 2018, the Partnership classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through other comprehensive income (OCI), or through profit or loss), and
- those to be measured at amortized cost

The classification depends on the Partnership's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether the Partnership has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The Partnership reclassifies debt investments only when its business model for managing those assets changes.

Measurement

At initial recognition, the Partnership measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Debt instruments

Subsequent measurement of debt instruments depends on the Partnership's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Partnership classifies its debt instruments:

- *Amortized cost:* Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. Interest income from these financial assets is included in interest income using the effective interest rate method. Any gain or loss arising on derecognition is recognized directly in profit or loss and presented in other income (expense), together with foreign exchange gains and losses. Impairment losses are presented as a separate line item in the unaudited condensed consolidated statement of comprehensive income (loss).
- *FVOCI:* Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

losses, interest income and foreign exchange gains and losses which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from the deficit to profit or loss and recognized in other income (expense). Interest income from these financial assets is included in interest income using the effective interest rate method. Foreign exchange gains and losses are presented in other income (expense) and impairment expenses are presented as separate line item in the unaudited condensed consolidated statement of comprehensive income (loss).

- *FVPL*: Assets that do not meet the criteria for amortized cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognized in profit or loss and presented net within other income (expense) in the period in which it arises.

Equity instruments

The Partnership subsequently measures all equity investments at fair value. Where the Partnership's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognized in profit or loss as other income when the Partnership's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognized in other income (expense) in the unaudited condensed consolidated statement of comprehensive income (loss) as applicable. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

Impairment

Beginning January 1, 2018, the Partnership assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortized cost and FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

For trade receivables, the Partnership applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

- (iii) IFRS 2, Share-based Payments. In June 2016, the IASB issued an amendment to address (i) certain issues related to the accounting for cash settled awards, and (ii) the accounting for equity settled awards that include a "net settlement" feature in respect of employee withholding taxes. The adoption of this standard had no impact on the unaudited condensed consolidated financial statements.
- (iv) IFRIC 22, Foreign Currency Transactions and Advance Consideration. In November 2016, the IFRS Interpretation Committee issued an interpretation on how to determine the date of the transaction when applying the standard on foreign currency transactions, IAS 21. The interpretation applies where an entity either pays or receives consideration in advance for foreign currency-denominated contracts. The adoption of this standard had no significant impact on the unaudited condensed consolidated financial statements.
- (v) IAS 40, Investment Property. In December 2016, the IASB issued an amendment to clarify when assets are transferred to, or from, investment properties. The amendment clarified that to transfer to, or from, investment properties there must be a change in use. This change must be supported by evidence. A change in intention, in isolation, is not enough to support a transfer. The adoption of this standard had no impact on the unaudited condensed consolidated financial statements.

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The impact of new standards, amendments to standards and interpretations that have been issued but not yet effective for financial periods beginning on or after January 1, 2019 and have not been early adopted have been discussed in the annual consolidated financial statements for the year ended December 31, 2017, except for the following:

- (i) IFRS 16, Leases. In January 2016, the IASB issued IFRS 16, Leases which replaces the current guidance in IAS 17, Leases. IFRS 16 requires lessees to recognize a right-of-use asset and a lease liability reflecting future lease payments for virtually all lease contracts. IFRS 16 must be applied to an entity's first annual IFRS financial statements for periods beginning on or after January 1, 2019, with early adoption permitted. Management can elect to adopt IFRS 16 using either the full retrospective approach or the modified retrospective approach.

Management has performed a preliminary assessment of IFRS 16 adoption and expects a significant impact on the consolidated financial statements. The right-of-use asset and lease liability are expected to be material to the consolidated statement of financial position. There is expected to be a change in presentation on the consolidated statement of comprehensive income (loss) and a significant impact on Adjusted EBITDA.

Management continues to evaluate the potential implications on data systems, internal controls over financial reporting, information technology, business processes, and financing and compensation arrangements. Management is also evaluating the transition approach it will apply and whether it will use the optional exemptions or practical expedients under the standard. Additional details, including the practical expedients elected and estimated quantitative impact on the consolidated financial statements are expected to be disclosed before the adoption of IFRS 16.

- (ii) IAS 19, Employee Benefits. In February 2018, the IASB issued an amendment in connection with defined benefit plans and accounting for plan amendments, settlements or curtailments. The mandatory effective date would be annual periods beginning on or after January 1, 2019, with early adoption permitted. Management is evaluating the amended standard and has not yet determined the impact on the unaudited condensed consolidated financial statements.
- (iii) IAS 28, Interests in Associates and Joint Ventures. In February 2018, the IASB issued an amendment to clarify that an entity applies IFRS 9, including its impairment requirements, to long term interests in an associate or joint venture to which the equity method is not applied. The mandatory effective date would be annual periods beginning on or after January 1, 2019, with early adoption permitted. Management is evaluating the amended standard and has not yet determined the impact on the unaudited condensed consolidated financial statements.

4 Critical accounting estimates and judgments

The preparation of these unaudited condensed consolidated financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities in the unaudited condensed consolidated financial statements and the disclosure of contingencies at the dates of the unaudited condensed consolidated statements of financial position, and the reported amounts of revenues and expenses during the reporting period. On a regular basis and with the information available, management reviews its estimates. Actual results could differ from those estimates. When adjustments become necessary, they are reported in earnings in the period in which they occur. The estimates and judgement applied by management that most significantly affect the unaudited condensed consolidated financial statements are the same as the ones that applied to the audited consolidated financial statements for the year ended December 31, 2017.

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

5 Other expense

	3-month period ended April 1, 2018	3-month period ended March 26, 2017
	\$	\$
Foreign exchange gain	(241)	(584)
Change in amortized cost of Partnership units liability	2,678	2,529
Change in fair value of derivatives	(649)	-
	<u>1,788</u>	<u>1,945</u>

6 Property, plant and equipment

	Land \$	Buildings \$	Machinery and equipment \$	Assets under construction or development \$	Total \$
As of January 1, 2018					
Cost	37,968	195,832	1,127,282	19,269	1,380,351
Accumulated depreciation and impairments	-	(84,897)	(533,844)	-	(618,741)
Net book value as of January 1, 2018	37,968	110,935	593,438	19,269	761,610
Additions	-	-	-	8,656	8,656
Disposals	(116)	-	(434)	-	(550)
Transfers	-	262	7,850	(8,112)	-
Depreciation	-	(1,253)	(10,230)	-	(11,483)
Exchange differences	39	1,489	8,465	63	10,056
As of April 1, 2018	<u>37,891</u>	<u>111,433</u>	<u>599,089</u>	<u>19,876</u>	<u>768,289</u>
As of April 1, 2018					
Cost	37,891	197,956	1,144,833	19,876	1,400,556
Accumulated depreciation and impairment	-	(86,523)	(545,744)	-	(632,267)
Net book value as of April 1, 2018	<u>37,891</u>	<u>111,433</u>	<u>599,089</u>	<u>19,876</u>	<u>768,289</u>

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Notes to Unaudited Condensed Consolidated Financial Statements

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

7 Pensions and post-retirement benefits

The following were the significant assumptions for the defined benefit pension plans and other benefit plans:

	Pensions		Post-retirement benefit plans	
	April 1, 2018	December 31, 2017	April 1, 2018	December 31, 2017
	%	%	%	%
Assumptions				
Discount rate - accrued benefit obligation	3.43	3.36	3.43	3.36
Rate of compensation increases	3.25 - 4.00	3.25 - 4.00		

The net benefit pension plan expense included the following components:

	Pensions		Post-retirement benefit plans	
	3-month period ended April 1, 2018	3-month period ended March 26, 2017	3-month period ended April 1, 2018	3-month period ended March 26, 2017
	\$	\$	\$	\$
Net benefit plan expense				
Current service cost	2,667	1,956	518	433
Interest cost	5,360	5,127	461	444
Expected return on plan assets	(4,364)	(4,345)	-	-
Administrative cost	159	124	-	-
	<u>3,822</u>	<u>2,862</u>	<u>979</u>	<u>877</u>

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

8 Provisions

	Environmental and asset retirement obligations \$ (a)	Long-term incentives \$ (b)	Restructuring \$	Total \$
Provisions as of January 1, 2018	5,191	1,062	53	6,306
Current	-	280	53	333
Non-current	5,191	782	-	5,973
Provisions as of January 1, 2018	5,191	1,062	53	6,306
Additional provisions	-	48	-	48
Paid during the period	-	-	(41)	(41)
Interest accretion	53	-	-	53
Provisions as of April 1, 2018	5,244	1,110	12	6,366
Current	-	268	12	280
Non-current	5,244	842	-	6,086

(a) Environmental and asset retirement obligations

The Partnership has made a provision for the potential obligation under a land lease at one of its plant locations to demolish the building and restore the land at the end of the lease to its original condition. The current lease ends in 2028 but an extension is currently being negotiated. The estimated undiscounted amount to settle this obligation would be between \$8.1 million and \$10.7 million. The liability is estimated using a discounted cash flow with a discount rate of 4.165% (December 31, 2017 – 4.165%).

(b) Long-term incentives

Long-term incentives include the Executive Long-Term Incentive Plan (LTIP) for the Partnership. The LTIP uses performance share units and results are based primarily on Adjusted EBITDA return on capital employed using a three year average, along with other components. The LTIP is paid in cash in May of the year following the three year period it is earned. The compensation expense is recognized over the same three year period.

9 Distributions and Partnership units liability

	Partnership units liability \$
As of January 1, 2018	160,309
Change in amortized cost of Partnership units liability (note 5)	2,678
Tax Distributions	(1,928)
As of April 1, 2018	161,059

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

The Partnership unit distributions paid, the portion of the distribution reinvested by the partners, the additional Partnership units issued at the unit price, and the gross proceeds were as follows:

<u>Distribution Payment Date</u>	3-month period ended April 1, 2018			
	Partnership unit distributions	Unit price	Issuance of Partnership units	Gross proceeds
	\$	\$	#	\$
January 15, 2018	10,382	13.50	361,174	4,876

<u>Distribution Payment Date</u>	3-month period ended March 26, 2017			
	Partnership unit distributions	Unit price	Issuance of Partnership units	Gross proceeds
	\$	\$	#	\$
January 16, 2017	10,148	15.25	309,196	4,715

On April 16, 2018, the Partnership paid a distribution of \$10.4 million to partners. Pursuant to the Partnership's Distribution Reinvestment Plan (DRIP), a portion of the distribution was reinvested by the partners, resulting in the Partnership issuing 457,788 Partnership units at a price of \$10.70. During the 3-month period ended April 1, 2018, a fair value adjustment of \$0.2 million was recorded to reflect the market value of the Partnership units issued.

Subsequent to April 1, 2018, the Partnership declared a distribution of \$10.5 million, payable on July 16, 2018.

The Partnership paid Partnership unit distributions, Tax Distributions and advances to its related parties as follows:

	3-month period ended April 1, 2018		
	Advances paid	Partnership unit distributions	Total
	\$	\$	\$
Paid to Kruger Inc. ^(a)	1,275	4,361	5,636
Paid to KPGP	-	1	1
Paid to KPT ^(b)	244	1,144	1,388
Total paid	1,519	5,506	7,025

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Notes to Unaudited Condensed Consolidated Financial Statements

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

	3-month period ended March 26, 2017			
	Tax	Advances	Partnership	Total
	Distributions	paid	unit	
	\$	\$	\$	\$
Paid to Kruger Inc. ^(a)	2,665	368	4,256	7,289
Paid to KPGP	-	-	1	1
Paid to KPT ^(b)	481	71	1,176	1,728
Total paid	3,146	439	5,433	9,018

(a) During the 3-month periods ended April 1, 2018 and March 26, 2017, Partnership unit distributions were paid to Kruger Inc. net of the DRIP reinvestment. During the 3-month period ended April 1, 2018, Kruger Inc.'s DRIP reinvestment was \$4.4 million (3-month period ended March 26, 2017 - \$4.3 million).

(b) During the 3-month periods ended April 1, 2018 and March 26, 2017, Partnership unit distributions were paid to KPT net of the DRIP reinvestment. During the 3-month period ended April 1, 2018, KPT's DRIP reinvestment was \$0.5 million (3-month period ended March 26, 2017 - \$0.4 million).

Tax Distributions

On February 28, 2018, KPLP declared a Tax Distribution of \$1.9 million, of which \$0.3 million was used to partially settle the advance to KPT recorded during the year ended December 31, 2017, and \$1.6 million was used to partially settle the advances to Kruger Inc. and KPGP recorded during the year ended December 31, 2017. The excess advances over the Tax Distributions in the amount of \$4.5 million, of which \$0.7 million are repayable by KPT and \$3.8 million are repayable by Kruger Inc. and KPGP, are due to KPLP by March 31, 2019.

During the 3-month period ended April 1, 2018, pursuant to the Tax Distribution as defined in the Partnership Agreement, the Partnership made advances to its partners of \$1.5 million, of which \$0.2 million was used to pay the monthly tax instalment on behalf of KPT and the remaining was advanced to Kruger Inc. and KPGP. The advances are non-interest bearing and non-recourse in nature and will be settled when the Tax Distribution is declared annually.

10 Income taxes

The Partnership is not a tax paying entity for the 3-month periods ended April 1, 2018 and March 26, 2017. The income from the Partnership flows to the partners, Kruger Inc., KPGP, and KPT. However, the Partnership's subsidiaries Kruger Products (USA) Inc., K.T.G. (USA) Inc., TAD Canco Inc., Grupo Tissue de Mexico S de RL de CV and TAD Luxembourg S.A.R.L. are corporate entities and, therefore, are subject to tax.

Income tax expense (recovery) was recognized based on management's best estimate of the weighted average annual income tax rate expected for the full financial year. The estimated weighted average annual income tax rate for the 3-month period ended April 1, 2018 was (199.2)% (3-month period ended March 26, 2017 – 27.3%).

Kruger Products L.P.

Notes to Unaudited Condensed Consolidated Financial Statements

For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

The components of income taxes were as follows:

	3-month period ended April 1, 2018	3-month period ended March 26, 2017
	\$	\$
Current tax expense	446	585
Deferred tax expense (recovery)	(1,496)	2,029
	<u>(1,050)</u>	<u>2,614</u>

11 Related party transactions

The Partnership makes sales to and acquires goods and services from Kruger Inc. and its subsidiary companies (related parties) in the normal course of business. These transactions are measured at the exchange amount, which is the amount agreed on by the related parties, and are non-interest bearing.

Sales of goods to Kruger Inc. for the 3-month period ended April 1, 2018 were \$0.1 million (3-month period ended March 26, 2017 - \$0.1 million). Goods are sold based on the price lists in force and terms that would be available to third parties.

Purchases of goods and services from Kruger Inc. for the 3-month period ended April 1, 2018 were \$1.7 million (3-month period ended March 26, 2017 - \$1.9 million). Purchases of goods and services from subsidiaries of Kruger Inc. for the 3-month period ended April 1, 2018 were \$8.8 million (3-month period ended March 26, 2017 - \$9.1 million). Goods are purchased from Kruger Inc. and related parties under normal commercial terms and conditions. These purchases of goods and services are included within cost of sales and selling, general and administrative expenses in the unaudited condensed consolidated statement of comprehensive income. During the 3-month period ended April 1, 2018, management fees of \$1.1 million (3-month period ended March 26, 2017 - \$1.1 million) were paid to Kruger Inc. for management services provided to the Partnership.

Balances due to and from related parties were as follows:

	April 1, 2018	December 31, 2017
	\$	\$
Receivables from Kruger Inc.	2	33
Receivables from KPT	52	52
	<u>54</u>	<u>85</u>
Payables to Kruger Inc.	7,165	999
Payables to subsidiaries of Kruger Inc.	1,122	1,597
	<u>8,287</u>	<u>2,596</u>

The receivables from and payables to related parties are based on commercial terms agreed on between the parties, unsecured and non-interest bearing. There were no provisions related to the receivables from related parties as of April 1, 2018 and December 31, 2017. There were no loans outstanding with related parties as of April 1, 2018 and December 31, 2017.

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The Partnership had declared distributions which are payable to its related parties as follows:

	April 1, 2018	December 31, 2017
	\$	\$
Distribution payable to Kruger Inc.	8,781	8,723
Distribution payable to KPGP	1	1
Distribution payable to KPT	1,665	1,658
Total distribution payable	<u>10,447</u>	<u>10,382</u>

12 Segment information

Reportable segments

Management has determined the operating segments based on the reports reviewed by the Chief Executive Officer who is considered to be the Chief Operating Decision Maker. The Partnership operates in three industry segments: Consumer, AFH and Other.

(a) Consumer

This segment operates using the Partnership's manufacturing facilities in Canada (New Westminster, British Columbia; Crabtree, Quebec; Sherbrooke, Quebec; Gatineau, Quebec) and in the United States (Memphis, Tennessee). The Consumer segment includes sales of branded tissue products such as Cashmere™, Purex™, White Swan™, Scotties™, Sponge Towels™ and White Cloud™ and private label tissue products.

(b) AFH

This segment operates using the Partnership's manufacturing facilities in Canada. The AFH business sells tissue products primarily through distributors to businesses involved in property management, health care, food service, manufacturing and lodging and also to public facilities.

(c) Other

This segment includes sales of parent rolls by the Partnership to other tissue manufacturing companies primarily in the United States and also in Canada and sales of recycled fibre primarily to its parent company. It also includes start-up costs related to capital projects, and certain corporate costs.

Segment operating income is the earnings (loss) for each such segment before (i) interest expense, (ii) income taxes, (iii) depreciation, (iv) amortization, (v) impairment (gain on sale) of non-financial assets, (vi) loss (gain) on disposal of property, plant and equipment, (vii) foreign exchange loss (gain), (viii) costs related to restructuring activities, (ix) changes in amortized cost of Partnership units liability, (x) change in fair value of derivatives, and (xi) one-time costs due to pension revaluations related to past service. "Consumer Segment Adjusted EBITDA", "AFH Segment Adjusted EBITDA" and "Other Segment Adjusted EBITDA" means in each case the Segment operating income for the respective reportable segment of KPLP.

The Partnership's assets, operations and employees are located primarily in Canada and the United States. The same long-term assets of the Partnership are used for the Consumer, AFH and Other segments. Accordingly, assets cannot be allocated to these segments.

Kruger Products L.P.

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For the 3-month periods ended April 1, 2018 and March 26, 2017

(tabular amounts are in thousands of Canadian dollars, except unit amounts)

	3-month period ended April 1, 2018			
	Consumer	AFH	Other	Total
	\$	\$	\$	\$
Revenue from external customers	267,696	53,525	2,514	323,735
Segment Adjusted EBITDA	29,871	(331)	(2,583)	26,957
Depreciation and amortization				13,110
Interest expense				11,313
Change in amortized cost of Partnership units liability				2,678
Change in fair value of derivatives				(649)
Loss on sale of property, plant and equipment				434
Gain on sale of non-financial assets				(215)
Foreign exchange gain				(241)
Income before income taxes				527
Income taxes				(1,050)
Net income				<u>1,577</u>

	3-month period ended March 26, 2017			
	Consumer	AFH	Other	Total
	\$	\$	\$	\$
Revenue from external customers	238,927	48,674	1,670	289,271
Segment Adjusted EBITDA	32,972	655	155	33,782
Depreciation and amortization				11,988
Interest expense				10,264
Change in amortized cost of Partnership units liability				2,529
Gain on sale of property, plant and equipment				(2)
Loss on sale of non-financial assets				13
Restructuring costs, net				11
Foreign exchange gain				(584)
Income before income taxes				9,563
Income taxes				2,614
Net income				<u>6,949</u>

Geographic segments

The Partnership operates in Canada, the United States and Mexico. Revenue and assets were allocated to geographic segment based on the location of the customer and long-term assets, respectively.

Revenue	3-month period ended April 1, 2018	3-month period ended March 26, 2017
	\$	\$
Canada	188,653	173,877
US	115,552	104,649
Mexico	19,530	10,745
	<u>323,735</u>	<u>289,271</u>

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

	April 1, 2018			
	Canada	US	Mexico	Total
	\$	\$	\$	\$
Property, plant and equipment	397,628	370,620	41	768,289
Goodwill	160,939	-	-	160,939
Intangible assets	15,032	-	-	15,032

	December 31, 2017			
	Canada	US	Mexico	Total
	\$	\$	\$	\$
Property, plant and equipment	397,133	364,435	42	761,610
Goodwill	160,939	-	-	160,939
Intangible assets	15,327	-	-	15,327

13 Financial instruments

Classification of financial instruments

As of April 1, 2018, the classification of the financial instruments, as well as their carrying amounts and fair values, was as follows:

	Classification	Carrying amount	Fair Value
		\$	\$
Cash and cash equivalents	financial assets at amortized cost	10,477	10,477
Trade and other receivables	financial assets at amortized cost	137,724	137,724
Receivables from related parties	financial assets at amortized cost	54	54
Advances to partners	financial assets at amortized cost	6,008	6,008
Derivative assets, net	financial assets at fair value through profit and loss	243	243
Bank indebtedness	financial liabilities at amortized cost	(9,140)	(9,140)
Trade payables	financial liabilities at amortized cost	(97,320)	(97,320)
Accrued expenses	financial liabilities at amortized cost	(59,107)	(59,107)
Contract liabilities	financial liabilities at amortized cost	(37,660)	(37,660)
Payables to related parties	financial liabilities at amortized cost	(8,287)	(8,287)
Distributions payable	financial liabilities at amortized cost	(10,447)	(10,447)
Long-term debt	financial liabilities at amortized cost	(460,520)	(463,480)
Partnership units liability	financial liabilities at amortized cost	(161,059)	(161,059)

The following table details the fair value hierarchy of financial instruments by level as of April 1, 2018:

	Level 1	Level 2	Level 3	Total
	\$	\$	\$	\$
Derivative assets, net	-	243	-	243
Long-term debt	-	(463,480)	-	(463,480)
Partnership units liability	-	-	(161,059)	(161,059)

Kruger Products L.P.

Notes to Unaudited Condensed Consolidated Financial Statements

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(tabular amounts are in thousands of Canadian dollars, except unit amounts)

As of December 31, 2017, the classification of the financial instruments, as well as their carrying amounts and fair values, was as follows:

	Classification	Carrying amount \$	Fair Value \$
Cash and cash equivalents	financial assets at amortized cost	8,837	8,837
Trade and other receivables	financial assets at amortized cost	113,194	113,194
Receivables from related parties	financial assets at amortized cost	85	85
Advances to partners	financial assets at amortized cost	6,417	6,417
Bank indebtedness	financial liabilities at amortized cost	(9,051)	(9,051)
Trade payables	financial liabilities at amortized cost	(104,558)	(104,558)
Accrued expenses	financial liabilities at amortized cost	(47,283)	(47,283)
Contract liabilities	financial liabilities at amortized cost	(38,493)	(38,493)
Derivative liabilities	financial liabilities at fair value through profit and loss	(364)	(364)
Payables to related parties	financial liabilities at amortized cost	(2,596)	(2,596)
Distributions payable	financial liabilities at amortized cost	(10,382)	(10,382)
Long-term debt	financial liabilities at amortized cost	(416,315)	(419,940)
Partnership units liability	financial liabilities at amortized cost	(160,309)	(160,309)

The following table details the fair value hierarchy of financial instruments by level as of December 31, 2017:

	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
Derivative liabilities	-	(364)	-	(364)
Long-term debt	-	(419,940)	-	(419,940)
Partnership units liability	-	-	(160,309)	(160,309)

Fair value

Cash and cash equivalents, trade and other receivables, receivables from related parties, advances to partners, bank indebtedness, trade payables, accrued expenses, contract liabilities, payables to related parties and distributions payable are short-term financial instruments whose fair value approximates the carrying amount, given they will mature in the near future. As of April 1, 2018, the fair values of the Credit Facility, the Nordea Facility and the Caisse Facility were \$220.1 million, \$17.0 million and \$189.1 million (December 31, 2017 – \$182.0 million, \$16.6 million and \$183.9 million), respectively, which approximates the current principal amount outstanding as the interest rate approximates current market interest rates. As of April 1, 2018, the fair values of the Quebec PM Loan and the Ontario Loan were \$34.8 million and \$2.5 million (December 31, 2017 – \$34.9 million and \$2.5 million), respectively, which are recorded on discounted future cash flows using a market rate of 4.4%, net of the government grant recorded on the below-market rate of interest.

The fair value of the derivative assets/liabilities was based on foreign exchange rates and interest rates in the active market. The change in the fair value of the derivative assets/liabilities based on foreign exchange rates was \$0.6 million gain during the 3-month period ended April 1, 2018 (3-month period ended March 26, 2017 – nil), which was recorded in the unaudited condensed consolidated statement of comprehensive income in Other expense. The valuation methodology used was categorized as a Level 2 methodology. The change in the fair value of the derivative assets/liabilities based on interest rates was \$0.04 million loss during the 3-month period ended April 1, 2018 (3-month period ended March 26, 2017 – nil), which was recorded in the unaudited condensed consolidated statement of comprehensive income in Interest expense. The valuation methodology used was categorized as a Level 2 methodology.

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Fair value of the Partnership units liability

The Partnership units liability is classified as a financial liability at amortized cost. Management has estimated the fair value of the Partnership units liability using a discounted cash flow model. Significant assumptions include the income tax obligation, discount rate and an industry capitalization rate. There were no significant changes in the assumptions during the 3-month period ended April 1, 2018.

Currency risk

The Partnership uses derivative financial instruments to manage foreign currency risk. Foreign exchange swaps and foreign exchange forwards are used to manage U.S. dollar borrowings. As of April 1, 2018, the Partnership had foreign exchange swaps outstanding of \$9.7 million (December 31, 2017 – \$31.5 million) and foreign exchange forwards outstanding of \$6.2 million (December 31, 2017 – \$19.0 million) with settlement dates ranging from April 4, 2018 to April 12, 2018.

Liquidity risk

As of April 1, 2018, the Caisse Facility, which matures on August 16, 2018, has been classified as short-term debt, resulting in a working capital deficit. Management fully expects to refinance all or part of the indebtedness prior to the maturity date. The Partnership has an executed engagement letter and confidential term sheet with a potential lender syndicate, with whom the Partnership is in the process of refinancing. Subject to refinancing being obtained, the Partnership believes its cash flows generated from operations combined with its available cash and credit facilities provide sufficient funding to meet its obligations.

Interest rate risk

The Partnership holds interest rate swaps, contracted to fix the interest rate on a notional amount of \$100.0 million at April 1, 2018 (December 31, 2017 – nil). The interest rate swaps are maturing during the 3-month period ended March 2020.

14 Cash and cash equivalents

	April 1, 2018	December 31, 2017
	\$	\$
Cash and cash equivalents	10,477	8,837
Bank indebtedness	(9,140)	(9,051)
Cash and cash equivalents in the unaudited condensed consolidated statement of cash flows	<u>1,337</u>	<u>(214)</u>

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15 Non-cash working capital

The change in non-cash working capital on the unaudited condensed consolidated statement of cash flows comprised the following:

	3-month period ended April 1, 2018	3-month period ended March 26, 2017
	\$	\$
Decrease (increase) in trade and other receivables	(19,807)	9,205
Decrease (increase) in receivables from related parties	31	(333)
Increase in inventories	(18,245)	(3,749)
Increase in prepaid expenses	(6,702)	(5,025)
Decrease in other long-term assets	-	130
Decrease in income taxes	292	864
Increase (decrease) in trade and other payables	2,119	(30,924)
Increase in payables to related parties	5,691	972
	<u>(36,621)</u>	<u>(28,860)</u>

16 Subsequent event

a) Senior unsecured notes

On April 24, 2018, the Partnership issued \$125 million in an aggregate principal amount of 6.0% senior unsecured notes due April 24, 2025 (the Notes) through a private placement. Interest on the Notes is payable in equal instalments on April 24 and October 24 of each year, commencing October 24, 2018. The Partnership may, at its option, redeem all or part of the Notes at any time prior to April 24, 2021 at an applicable redemption premium and on or after April 24, 2021 at fixed redemption prices plus, in each case, accrued and unpaid interest, if any, to the applicable redemption date. If the Partnership undergoes a change in control, it will be required to offer to purchase the Notes.

The Notes include an early repayment option. The Partnership has determined that the early repayment option is an embedded derivative that is not closely related to the Notes. Accordingly, it is expected that the embedded derivative will be bifurcated from the Notes for financial reporting purposes.

The Notes are senior unsecured obligations of the Partnership. The Notes rank senior in right of payment to all existing and future subordinated indebtedness of the Partnership and equal in right of payment to all indebtedness of the Partnership that is not subordinated in right of payment to the Notes other than any indebtedness of the Partnership, including the Credit Facility and the Nordea Facility, to the extent of the assets securing such indebtedness. The Notes are unconditionally guaranteed, jointly and severally, by the Restricted Subsidiaries.

The net proceeds from the offering were approximately \$122 million after deducting fees payable to the underwriters and related expenses. The Partnership used the net proceeds of the offering to reduce the outstanding balance under the Credit Facility.

b) Revolving credit facility

On April 24, 2018, the Partnership entered into the sixth amended and restated credit agreement (the Credit Agreement) related to its revolving credit facility (the Credit Facility). The Credit Facility was reduced to \$200.0 million from \$300.0 million. The borrowings under the Credit Facility bear interest at a base rate of Canadian prime rate, U.S. base rate, banker's acceptance rates or LIBOR, plus a margin varying between 0.20% and

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2.875% depending on the ratio of total net funded debt to EBITDA (as defined in the Credit Agreement) and the type of advance. The Credit Agreement is for a five year period and will mature on April 24, 2023. The Credit Agreement provides for certain restrictive undertakings and covenants to be complied with by the Partnership.

The Credit Agreement is guaranteed by KPLP, KPGP, Kruger Products Real Estate Holdings Inc., Grupo Tissue De Mexico S de RL de CV, Kruger Products (USA) Inc., Kruger Products AFH G.P. Inc. and Kruger Products AFH L.P. and their respective subsidiaries (the Restricted Subsidiaries). The Partnership and the Restricted Subsidiaries provide first ranking security interests and hypothecs over their current and future tangible assets to secure the obligations under the Credit Agreement including a pledge of 100% of the stock or ownership interest in all subsidiaries owned by the Partnership and the Restricted Subsidiaries.

c) Nordea facility

On April 24, 2018, the Partnership entered into the fourth amended credit agreement (the Nordea Credit Agreement) related to its Nordea Facility, in connection with amendments to the Credit Facility. No significant changes were made to the Nordea Facility.