BOWATER CANADIAN FOREST PRODUCTS INC.

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2008

Prepared by Management without Auditor Review

See Notice to Reader

Notice to Reader

Management has compiled the unaudited interim financial information of Bowater Canadian Forest Products Inc., consisting of the comparative Consolidated Balance Sheets as of September 30, 2008 and December 31, 2007 and the comparative Consolidated Statements of Operations, Deficit, Cash Flows and Comprehensive Loss for the three and nine months ended September 30, 2008 and 2007. All amounts are stated in Canadian dollars, unless otherwise indicated. An auditor has not reviewed or audited these interim consolidated financial statements.

Bowater Canadian Forest Products Inc.

(Unaudited interim consolidated financial statements)

Three and nine months ended September 30, 2008

Bowater Canadian Forest Products Inc.
Consolidated Statements of Operations
(Unaudited, in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Sales	**$ 314**	$ 322	**$ 916**	$ 1,056
Costs and expenses				
Cost of sales, excluding depreciation, amortization and cost of timber harvested	**260**	303	**814**	936
Depreciation, amortization and cost of timber harvested	**29**	40	**103**	121
Distribution costs	**39**	38	**109**	122
Selling and administrative expenses	**2**	14	**34**	44
Closure costs, impairment and other related charges	**194**	-	**208**	-
	524	395	**1,268**	1,223
Operating loss	**(210)**	(73)	**(352)**	(167)
Interest expense, net	**(10)**	(11)	**(30)**	(33)
Other income (expense), net	**5**	(39)	**(5)**	(42)
Loss before income taxes	**(215)**	(123)	**(387)**	(242)
Income tax benefit (provision)	**-**	1	**2**	(2)
Net loss	**$ (215)**	$ (122)	**$ (385)**	$ (244)

Consolidated Statements of Deficit
(Unaudited, in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Deficit at beginning of period				
As previously reported	**$ (2,290)**	$ (1,700)	**$ (2,104)**	$ (1,578)
Correction of an error in cost of sales in prior periods	**-**	-	**(16)**	-
As restated – Note 1	**(2,290)**	(1,700)	**(2,120)**	(1,578)
Net loss	**(215)**	(122)	**(385)**	(244)
Dividends declared	**-**	(1)	**-**	(1)
Deficit at end of period	**$ (2,505)**	$ (1,823)	**$ (2,505)**	$ (1,823)

See accompanying notes to unaudited consolidated financial statements.

Bowater Canadian Forest Products Inc.
Consolidated Balance Sheets
(Unaudited, in millions)

	September 30, 2008	December 31, 2007 Restated – Note 1
Assets		
Current Assets		
Cash and cash equivalents	$ 5	$ 14
Accounts receivable, net		
Trade	81	98
Other	12	56
Affiliates	34	15
Income and other taxes receivable	-	4
Inventories	150	178
Assets held for sale	56	5
Prepaid expenses	9	5
Total current assets	347	375
Advances to affiliates	361	329
Fixed assets, net	750	1,174
Assets held for sale	127	1
Goodwill	8	9
Other assets	132	138
Total assets	$ 1,725	$ 2,026
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable and accrued liabilities	$ 155	$ 201
Short-term bank debt	71	-
Current installments of long-term debt	13	20
Liabilities associated with assets held for sale	23	-
Total current liabilities	262	221
Advances from affiliates	420	357
Long-term debt, net of current portion	217	225
Pension and postretirement benefit obligations	95	104
Non-controlling interest in subsidiary	6	6
Liabilities associated with assets held for sale	26	-
Other liabilities	15	14
Total liabilities	1,041	927
Commitments and contingencies		
Shareholders' equity		
Common and preferred stock	2,663	2,663
Additional paid-in capital	568	568
Accumulated other comprehensive loss	(42)	(12)
Deficit	(2,505)	(2,120)
Total shareholders' equity	684	1,099
Total liabilities and shareholders' equity	$ 1,725	$ 2,026

See accompanying notes to unaudited consolidated financial statements.

Bowater Canadian Forest Products Inc.
Consolidated Statements of Cash Flows
(Unaudited, in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Cash flows from operating activities:				
Net loss	**$ (215)**	$ (122)	**$ (385)**	$ (244)
Adjustments to reconcile net loss to net cash used in operating activities:				
Depreciation, amortization and cost of timber harvested	**29**	40	**103**	121
Future income taxes	**-**	(1)	**(1)**	2
Net loss (gain) on disposition of assets	**-**	-	**1**	(18)
Closure costs, impairment and other related charges	**194**	-	**205**	-
Unrealized exchange loss (gain) on long-term monetary items	**15**	(25)	**27**	(54)
Changes in net assets or liabilities of pension and other postretirement benefit plans	**(12)**	(16)	**(16)**	(16)
Other, net	**(9)**	(7)	**(20)**	(15)
Net change in working capital, excluding cash	**(17)**	122	**(3)**	77
Net cash used in operating activities	**(15)**	(9)	**(89)**	(147)
Cash flows from investing activities:				
Cash invested in fixed assets, timber and timberlands	**(3)**	(8)	**(16)**	(30)
(Advances to) repayments from affiliates	**(26)**	29	**(35)**	74
Disposition of assets, including timber and timberlands	**7**	-	**12**	27
Net cash (used in) provided by investing activities	**(22)**	21	**(39)**	71
Cash flows from financing activities:				
Increase (decrease) in bank overdraft and short-term bank debt	**30**	(10)	**71**	(5)
Repayment of long-term debt	**-**	-	**(21)**	(15)
Dividends	**-**	(1)	**-**	(1)
Advances from affiliates	**11**	-	**69**	98
Net cash provided by (used in) financing activities	**41**	(11)	**119**	77
Net increase (decrease) in cash and cash equivalents	**4**	1	**(9)**	1
Cash and cash equivalents, beginning of period	**1**	-	**14**	-
Cash and cash equivalents, end of period	**$ 5**	$ 1	**$ 5**	$ 1
Supplemental disclosures of cash flow information:				
Cash paid during the period for:				
Interest, including capitalized interest	**$ 7**	$ 8	**$ 22**	$ 29

See accompanying notes to unaudited consolidated financial statements.

Bowater Canadian Forest Products Inc.
Consolidated Statements of Comprehensive Loss
(Unaudited, in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Net loss	**$ (215)**	$ (122)	**$ (385)**	$ (244)
Other comprehensive (loss) income:				
Exchange translation of foreign subsidiaries	**(14)**	(26)	**(30)**	(28)
Comprehensive loss	**$ (229)**	$ (148)	**$ (415)**	$ (272)

See accompanying notes to unaudited consolidated financial statements.

1. Organization and Basis of Presentation

Basis of Presentation

The accompanying consolidated financial statements include the accounts of Bowater Canadian Forest Products Inc. and its subsidiaries (collectively referred to as "we," "us," "our," and the "Company"). We are a wholly-owned subsidiary of AbitibiBowater Canada Inc., which is an indirect subsidiary of Bowater Incorporated ("Bowater"). On October 29, 2007, Bowater combined with Abitibi-Consolidated Inc. ("Abitibi") in a merger of equals (the "Combination"). As a result of the Combination, Bowater and Abitibi each became a wholly-owned subsidiary of AbitibiBowater Inc. ("AbitibiBowater").

These financial statements are expressed and denominated in Canadian dollars except where otherwise noted and have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). The consolidated balance sheets, statements of operations, deficit, cash flows and comprehensive loss are unaudited. However, in management's opinion, all adjustments (consisting of normal recurring adjustments) necessary for fair presentation of these unaudited interim consolidated financial statements have been made. The results of the interim period ended September 30, 2008 are not necessarily indicative of the results expected for the full year. These unaudited interim consolidated financial statements and notes should be read in conjunction with our audited annual consolidated financial statements and accompanying notes for the year ended December 31, 2007, filed on April 29, 2008.

Restatement

During the first quarter of 2008, we restated our consolidated balance sheet as of December 31, 2007 and opening deficit for the nine months ended September 30, 2008 in our consolidated statements of deficit to correct an error. During 2007, we understated our cost of sales by $16 million, which resulted in our operating loss and net loss being understated by $16 million. This error was associated with inventories transferred to Bowater America Inc. ("BAI"), a wholly-owned subsidiary of Bowater, at the end of 2006 and sold by BAI in 2007.

Adoption of New Accounting Standards

Capital disclosures

On January 1, 2008, we adopted the Canadian Institute of Chartered Accountants ("CICA") Accounting Standards Board ("AcSB") Section 1535 of the CICA Handbook, "Capital Disclosures." The capital disclosures standard establishes required disclosure of information about an entity's capital and how it is managed, including an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital, and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance.

Inventories

On January 1, 2008, we adopted Section 3031 of the CICA Handbook, "Inventories," which prescribes the accounting treatment for inventories. Section 3031 provides guidance on the determination of costs and its subsequent recognition as an expense and provides guidance on the cost formulas used to assign costs to inventories.

The standard introduces significant changes to the measurement and disclosure of inventory. The measurement changes include: the elimination of LIFO, the requirement to measure inventories at the lower of cost and net realizable value, the allocation of overhead based on normal capacity, the use of the specific cost method for inventories that are not ordinarily interchangeable or goods and services produced for specific purposes, the requirement for an entity to use a consistent cost formula for inventory of a similar nature and use and the reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories. Disclosures of inventories have also been enhanced. Inventory policies, carrying amounts, amounts recognized as an expense, write-downs and the reversals of write-downs are required to be disclosed.

Entities can choose to apply the standard either to opening inventory for the period, adjusting opening retained earnings by the difference in the measurement of opening inventory, or retrospectively by restating prior periods. The adoption of this standard had no significant impact on our consolidated financial position as we were already following most of the newly required practices.

Financial instruments – disclosure and presentation

In December 2006, the AcSB published the following two Sections of the CICA Handbook: Section 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation." These two Sections came into effect on January 1, 2008 replacing Section 3861, "Financial Instruments – Disclosures and Presentation." These changes are disclosed in Note 11, "Financial Instruments and Capital Management." The new standards introduce disclosure and presentation requirements that will enable financial statements' users to evaluate and enhance their understanding of the significance of financial instruments for the entity's financial position, performance and cash flows and the nature and extent of risks arising from financial instruments to which the entity is exposed and how those risks are managed. The existing requirements on presentation of financial instruments have been carried forward unchanged.

In addition, disclosure is required of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk, currency risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable.

Accounting Principles Issued but Not Yet Adopted

Goodwill and intangible assets

In February 2008, the AcSB issued Section 3064 of the CICA Handbook, "Goodwill and Intangible Assets," replacing Section 3062, "Goodwill and Other Intangible Assets," and Section 3450, "Research and Development Costs." The objectives of the new standard are to reinforce the principles-based approach to the recognition of costs as an asset under the current definition of assets and the recognition principles in the conceptual framework, and to clarify the application of the concept of matching revenues and expenses. The changes will be effective for fiscal years beginning on or after October 1, 2008. Earlier adoption is permitted. We are currently assessing the impact that these accounting pronouncements will have on our consolidated financial statements.

2. Closure Costs, Impairment and Other Related Charges

"Closure costs, impairment and other related charges" in the Consolidated Statements of Operations includes the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Unaudited, in millions)	**2008**	2007	**2008**	2007
Asset impairment	**$ 194**	$ -	**$ 194**	$ -
Other closure costs:				
Non-cancelable contracts	**-**	-	**10**	-
Severance and other	**-**	-	**4**	-
	$ 194	$ -	**$ 208**	$ -

Immediately upon the Combination, AbitibiBowater began a comprehensive strategic review of its operations to reduce costs and improve its profitability. On November 29, 2007, AbitibiBowater announced the results of the initial phase of its comprehensive review, which included a decision to reduce its newsprint and specialty papers production capacity by approximately one million metric tons per year. The reductions included the permanent closure of our Dalhousie, New Brunswick paper mill, as well as the indefinite idling of our Donnacona, Quebec paper mill. Additionally, AbitibiBowater decided to permanently close paper machine no. 3 at our Gatineau, Quebec facility. The actions were completed in the first quarter of 2008. We recorded charges of $157 million for long-lived asset impairment, severance and related costs associated with our mills in the fourth quarter of 2007. During the three and nine months ended September 30, 2008, we recorded an additional $6 million of asset impairment charges related to our Dalhousie facility. During the nine months ended September 30, 2008, we recorded additional costs for non-cancelable contracts of $10 million and severance and other costs of $4 million at our Dalhousie and Donnacona operations.

In November 2008, AbitibiBowater announced the permanent closure of our previously idled Donnacona paper mill, based on current market conditions. Upon review of the recoverability of the long-lived assets at this facility, we used this additional information and recorded long-lived asset impairment charges of $188 million at our Donnacona paper mill for the three and nine months ended September 30, 2008. The fair value of the long-lived assets of Donnacona of $15 million was determined based on its estimated sale and salvage values. Additionally, $7 million of mill stores inventory was determined to be unusable and was recorded in cost of sales.

3. Interest Expense, net

"Interest expense, net" in the Consolidated Statements of Operations includes the following:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
(Unaudited, in millions)	**2008**	2007	**2008**	2007
Interest on third party long-term debt	**$ (7)**	$ (7)	**$ (22)**	$ (22)
Net interest expense on advances from affiliates	**(3)**	(4)	**(9)**	(11)
Amortization of deferred financing costs	**-**	(1)	**-**	(1)
Interest income	**-**	1	**1**	1
	$ (10)	$ (11)	**$ (30)**	$ (33)

4. Other Income (Expense), net

"Other income (expense), net" in the Consolidated Statements of Operations includes the following:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
(Unaudited, in millions)	**2008**	2007	**2008**	2007
Foreign exchange gain (loss)	**$ 5**	$ (10)	**$ 2**	$ (32)
Net (loss) gain on disposition of assets	**-**	-	**-**	18
Arbitration award	**-**	(29)	**-**	(29)
Share in income of company subject to significant influence	**-**	-	**(7)**	-
Miscellaneous income	**-**	-	**-**	1
	$ 5	$ (39)	**$ (5)**	$ (42)

On September 7, 2007, we received a decision in an arbitration related to the 1998 sale to Weyerhaeuser Company ("Weyerhaeuser") of our former pulp and paper facility in Dryden, Ontario. We and Weyerhaeuser had been arbitrating a claim regarding the cost of certain environmental matters related to the mill. The arbitrators awarded Weyerhaeuser approximately $44 million, including interest. As a result of the arbitrator's decision, which is binding upon us and not subject to appeal, we recorded a pre-tax charge of $29 million during the three and nine months ended September 30, 2007. This amount is included above as "Arbitration award." We had previously established a reserve of approximately $15 million in connection with these environmental matters at the time of the sale.

5. Liquidity and Debt

Liquidity, Short-term Bank Debt and Current Installments of Long-term Debt

As of September 30, 2008, total short-term bank debt and current installments of long-term debt totaled $84 million. In order to address our upcoming debt maturities, which primarily consist of our Canadian bank credit facility, which matures on June 5, 2009 (US$67 million (CDN$71 million) outstanding as of September 30, 2008), we and Bowater are currently pursuing refinancing alternatives and the sale of assets.

Our primary sources of liquidity and capital resources are cash on hand, cash provided from operations and available borrowings under our bank credit facility. As of September 30, 2008, we had cash on hand of approximately $5 million. Our third quarter 2008 cash used in operations was $15 million, an improvement of $16 million as compared to the second quarter of 2008. In addition, we had US$46 million (CDN$49 million) of available borrowings under our bank credit facility as of September 30, 2008, subject to applicable collateral requirements and covenant restrictions.

There is no assurance that we will have sufficient cash to repay our bank credit facility due June 5, 2009, without significant asset sales or external financing as presently contemplated by our and Bowater's available refinancing plans. Bowater is currently seeking to replace both its U.S. credit facility and our Canadian credit facility with a senior secured asset-based revolving credit facility with a syndicate of lenders prior to March 31, 2009 and is exploring the feasibility of issuing senior secured notes contingent upon the consummation of the new asset-based revolving credit facility. The proceeds of any such notes offering would be used to repay certain indebtedness of Bowater and for working capital for Bowater and it subsidiaries, including us.

Bank Credit Facility

As of September 30, 2008, available borrowings under our bank credit facility were as follows:

(Unaudited, in millions)	Commitment	Amount Outstanding	Commitment Available (1)	Termination Date	Weighted Average Interest Rate (2)
Credit facility	$ 153	$ 71	$ 49	June 2009	6.3%

(1) The commitment available under the revolving bank credit facility is subject to collateral requirements and covenant restrictions (after giving effect to the financial covenant waivers included in the November 12, 2008 amendment) as described below or in our audited consolidated financial statements for the year ended December 31, 2007, filed on April 29, 2008, in our unaudited interim consolidated financial statements for the quarter ended March 31, 2008, filed on May 30, 2008 or in our unaudited interim consolidated financial statements for the quarter ended June 30, 2008, filed on August 29, 2008, and is reduced by outstanding letters of credit of US$31 million (CDN$33 million). Commitment fees for unused portions of our credit facility are 25 basis points.
(2) Borrowings under the bank credit facility incur interest based, at our option, on specified market interest rates plus a margin.

Our credit agreement is secured by liens on our inventory, accounts receivable and deposit accounts and is guaranteed by Bowater, Bowater Newsprint South LLC and certain of their wholly-owned subsidiaries and certain of our subsidiaries. Availability under the credit facility is limited to 60% of the net book value of our accounts receivable and inventory, including that of our subsidiaries, and is reduced by the amount of outstanding letters of credit.

Amendments to Bank Credit Facility

For a more complete discussion of our bank credit facility, as well as certain amendments to this facility entered into on November 2, 2007, February 25, 2008 and March 31, 2008, reference is made to our audited consolidated financial statements for the year ended December 31, 2007, filed on April 29, 2008, for the amendment to this bank credit facility entered into on May 28, 2008, reference is made to our unaudited interim consolidated financial statements for the quarter ended March 31, 2008, filed on May 30, 2008 and for amendments to this bank credit facility entered into on June 6, 2008 and August 7, 2008, reference is made to our unaudited interim consolidated financial statements for the quarter ended June 30, 2008, filed on August 29, 2008.

Under previous amendments, the lenders under the credit facility implemented a more restrictive borrowing base, using more extensive eligibility criteria and imposing additional reporting obligations on Bowater and us (although, as described below, the date by which we and Bowater must comply with these more restrictive requirements is now to be phased in through March 31, 2009).

On November 12, 2008, Bowater and the other parties to its U.S. credit facility and we and the other parties to our Canadian credit facility entered into amendments to those facilities that, among other things: (1) waive the requirement that we and Bowater are required to comply immediately with the more restrictive borrowing base requirements by November 15, 2008 and provide instead for phased-in implementation through March 31, 2009 (extending to April 29, 2009 under certain circumstances) and waive compliance with certain financial covenant requirements for the third quarter of 2008 (absent such waiver, we and Bowater would have been in violation of the senior secured leverage ratio and the interest coverage ratio covenants under the credit facilities for the third quarter); (2) amend certain covenants, including the leverage ratio, for the fourth quarter of 2008; (3) increase the interest rate under each facility by 125 basis points; (4) provide a lien on substantially all Canadian fixed assets and the shares of our South Korean subsidiary (which operates our Mokpo mill) to Canadian lenders, as security for indebtedness in a principal amount not to exceed 10% of our shareholders' equity as of September 30, 2008; (5) add a provision requiring that 75% of the proceeds of asset sales by Bowater or its subsidiaries, including us, be used to reduce amounts outstanding under both facilities on a pro rata basis; (6) reduce, pro rata, the aggregate amount of the commitment under both facilities by US$10 million; and (7) require that Bowater and certain of its affiliates (including us) maintain no more than $70 million of cash on hand on a combined consolidated basis, with any excess to be used to reduce amounts outstanding under the facilities.

We expect to be in compliance with the financial covenants of our amended credit facility through March 31, 2009. However, as discussed above, Bowater expects to refinance our Canadian credit facility prior to March 31, 2009. Bowater's ability to consummate such refinancing will be subject to market and other conditions, and no assurance can be made that such transactions will be consummated on terms acceptable to us or Bowater, or at all.

6. Pension and Other Postretirement Expense

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Unaudited, in millions)	**2008**	2007	**2008**	2007
Pension Plans:				
Components of net periodic benefit cost:				
Service cost	**$ 3**	$ 5	**$ 10**	$ 16
Interest cost	**21**	20	**62**	62
Expected return on plan assets	**(24)**	(23)	**(72)**	(67)
Amortization of transition obligation	**1**	-	**3**	-
Amortization of prior service cost	**-**	1	**2**	3
Recognized net actuarial loss	**2**	4	**5**	13
Special termination benefits	**-**	3	**1**	7
Curtailments and settlements	**1**	6	**10**	8
Other	**3**	-	**8**	2
Net periodic benefit cost	**$ 7**	$ 16	**$ 29**	$ 44
Other Postretirement Benefit Plans:				
Net periodic benefit cost	**$ 1**	$ 1	**$ 3**	$ 3

Events Impacting Net Periodic Benefit Cost for the Three and Nine Months Ended September 30, 2008

In March 2008, membership in our Canadian executive pension arrangements was restricted, effective January 1, 2009. As a result, a curtailment loss of approximately $1 million was included in the net periodic benefit cost of the pension plans for the nine months ended September 30, 2008.

In November 2007, we announced the permanent closure of our Dalhousie, New Brunswick mill. As a result, a curtailment loss of $8 million and special termination benefits of $1 million were included in the net periodic benefit cost of the pension plans, and a curtailment loss of $1 million was included in the net periodic benefit cost of the other postretirement benefit plans during the nine months ended September 30, 2008.

In November 2007, certain employees received lump-sum payouts from a retirement plan. Accordingly, a settlement loss of $1 million was included in the net periodic benefit cost of the pension plans during the nine months ended September 30, 2008.

Events Impacting Net Periodic Benefit Cost for the Three and Nine Months Ended September 30, 2007

In June 2007, union members at our Dolbeau, Quebec facility ratified a new labor agreement. As a result of a mill-wide restructuring of this facility, 130 jobs were eliminated. A curtailment loss of approximately $3 million was included in the net periodic benefit cost of our pension plans for the three and nine months ended September 30, 2007 as a result of the employee reduction.

In May 2007, union members at our Gatineau, Quebec facility ratified a new labor agreement. As a result of a mill-wide restructuring of this facility, 143 jobs were eliminated. A pension curtailment loss of approximately $3 million, special termination benefits of approximately $3 million and a non-pension post-retirement curtailment loss of less than $1 million were included in the net periodic benefit cost of our pension plans for the three and nine months ended September 30, 2007 as a result of the employee reduction.

In February 2007, as a result of a mill-wide restructuring of our Thunder Bay, Ontario facility, 157 jobs were eliminated. As a result, a pension curtailment loss of $2 million and special termination benefits of $4 million were included in the net periodic benefit cost of our pension plans during the nine months ended September 30, 2007. This event will also result in a settlement loss at the time the benefits are paid.

7. Income Taxes

Due to operating losses and an evaluation of available tax planning strategies, we record tax charges to establish valuation allowances against a substantial portion of our net future tax assets, which are primarily for tax loss carryforwards and tax credits. Additionally, we will likely not record income tax benefits on the majority of our future operating losses, which would have an adverse impact on our overall effective income tax rate in future periods.

8. Assets Held for Sale and Liabilities Associated with Assets Held for Sale

As of December 31, 2007, we held our Price, Quebec sawmill and approximately 64 acres of timberlands in Canada for sale. On March 23, 2008, we sold our Price sawmill to Groupe Lebel (2004) Inc. for proceeds of approximately $5 million, resulting in a net loss of approximately $1 million.

As of September 30, 2008, we were continuing to market for sale the timberlands in Canada and were also marketing our Mokpo, Korea newsprint facility and certain assets at our Ignace, Ontario sawmill. We expect to complete a sale of these assets within the next twelve months for an amount that exceeds their individual carrying values. The assets and liabilities held for sale are carried on our Consolidated Balance Sheets at the lower of carrying value or fair value less costs to sell. We cease recording depreciation and amortization when assets are classified as held for sale.

9. Segment Information

We manage our business based on the products that we manufacture and sell to external customers. Our reportable segments are newsprint, specialty papers, market pulp and lumber.

None of the income or loss items following "Operating loss" in our Consolidated Statements of Operations are allocated to our segments, since those items are reviewed separately by management. For the same reason, closure costs, impairment and other related charges, employee termination costs, net (losses) gains on dispositions of assets and other discretionary charges or credits are not allocated to the segments. We allocate depreciation expense to our segments, although the related fixed assets are not allocated to segment assets.

The following table summarizes information about segment sales and operating income (loss) for the three and nine months ended September 30, 2008 and 2007.

(Unaudited, in millions)		Newsprint	Specialty Papers	Market Pulp	Lumber	Corporate and Other	Consolidated Total
Sales							
Third Quarter	**2008**	**$ 170**	**$ 44**	**$ 58**	**$ 41**	**$ 1**	**$ 314**
Third Quarter	2007	141	75	60	46	-	322
Year to date	**2008**	**443**	**185**	**169**	**118**	**1**	**916**
Year to date	2007	478	263	169	146	-	1,056
Operating income (loss)(1)							
Third Quarter	**2008**	**$ 3**	**$ (6)**	**$ 7**	**$ (6)**	**$ (208)**	**$ (210)**
Third Quarter	2007	(35)	(24)	9	(10)	(13)	(73)
Year to date	**2008**	**(35)**	**(31)**	**7**	**(23)**	**(270)**	**(352)**
Year to date	2007	(54)	(47)	8	(28)	(46)	(167)

(1) "Corporate and Other" operating loss included closure costs, impairment and other related charges of $194 million and $208 million for the three and nine months ended September 30, 2008, respectively, related to the permanent closures of our Donnacona and Dalhousie paper mills. In addition, we recorded charges for the writedown of mill stores inventory related to the permanent closure of our Donnacona paper mill of $7 million for the three and nine months ended September 30, 2008.

10. Transactions with Related Parties

Bowater maintains a United States domestic sales force. Bowater and BAI buy products from us at the same price they sell those products to third party customers. During the three and nine months ended September 30, 2008, these sales amounted to $163 million and $481 million, respectively. During the three and nine months ended September 30, 2007, these sales amounted to $143 million and $501 million, respectively. Bowater has modified the methodology for charging a portion of its sales services from a commission-based charge to a service fee equal to 120% of their selling costs based on the value of the products acquired from us. For the three months ended September 30, 2008, we were charged less than $1 million for such services and for the nine months ended September 30, 2008, the aggregate charges for such services totaled $3 million. For the three and nine months ended September 30, 2007, these charges totaled $4 million and $15 million, respectively.

Bowater provides certain corporate administrative services on behalf of us and certain of its subsidiaries including legal, finance, tax, risk management, IT, executive management, payroll and employee benefits. During the nine months ended September 30, 2008, Bowater changed its methodology for allocating these corporate administrative services. We received a credit of less than $1 million for the three months ended September 30, 2008, and we were charged $10 million for the nine months ended September 30, 2008, less than $1 million for the three months ended September 30, 2007 and $1 million for the nine months ended September 30, 2007.

Additionally, we also receive other services from Bowater. The aggregate charges for such services during both the three and nine months ended September 30, 2008, and both the three and nine months ended September 30, 2007, were less than $1 million.

11. Financial Instruments and Capital Management

Please refer to the footnotes to our audited annual consolidated financial statements for the year ended December 31, 2007, filed on April 29, 2008, for additional information regarding our financial instruments.

Nature and Extent of Risks Arising from Financial Instruments

In the normal course of business, we are exposed to certain financial risks. Risk management is carried out by a central treasury department of AbitibiBowater under policies approved by the AbitibiBowater Board of Directors. This department identifies, evaluates and manages financial risks.

Credit Risk

We are exposed to credit risk on the accounts receivable from our customers. In order to manage our credit risk, we have adopted policies, which include the analysis of the financial position of our customers and the regular review of their credit limits. We have a large and diversified customer base, and as a result, do not have significant exposure to any individual customer. Our customers are mainly in the newspaper publishing, commercial printing, paper converting, advertising and lumber wholesaling and retailing businesses. Historically, credit losses have been low, and we provide for an allowance for doubtful accounts to absorb credit losses.

Liquidity Risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with its operations and financial liabilities. In order to manage this risk, we forecast the cash requirements over the near and long term to determine whether sufficient funds will be available. Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of our underlying businesses, we aim to maintain flexibility in funding by keeping either committed credit lines or sufficient funds available. Refer to Note 5, "Liquidity and Debt" for additional information regarding how we manage our liquidity risks.

The fair value of our financial assets approximates their carrying amounts. The following table summarizes the aggregate amount of contractual future cash flows for our financial liabilities, and their fair value, as of September 30, 2008.

	Carrying Value				
(Unaudited, in millions)	Total	1 - 3 Years	4 - 5 years	After 5 years	Fair Value
Long-term debt, net of current portion	$ 217	$ 92	$ -	$ 125	$ 93
Advances from affiliates	420	-	-	420	*

* The fair value cannot be determined due to the related-party nature of this instrument.

Foreign Exchange Risk

Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. We are exposed to foreign currency exchange rates, primarily arising from sales and purchases that are denominated in a currency other than the respective functional currencies of our foreign and domestic operations.

Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. We are exposed to interest rate risk on our variable-rate long-term debt and our short-term bank debt. Our objective is to manage the impact of interest rate changes on earnings and cash flows and on the market value of our borrowings. At September 30, 2008, approximately 76% of our debt was at fixed rates.
The following table summarizes our exposure to changes in interest rates and foreign currency on our financial assets and liabilities.

(Unaudited, in millions)	Carrying Amount	Interest Rate Risk Effect of 1% rate change[1]	Foreign Exchange Rate Risk Effect of 10% rate change[1]
Financial assets			
Cash and cash equivalents	$ 5	$ -	$ -
Accounts receivable	127	-	1
Current financial assets held for sale	30	-	3
Advances to affiliates	361	-	15
Financial liabilities			
Accounts payable and accrued liabilities	155	-	-
Current financial liabilities associated with assets held for sale	23	-	(2)
Short-term bank debt	71	(1)	(4)
Current installments of long-term debt	13	-	(2)
Long-term debt, net of current portion	217	-	(5)
Long-term financial liabilities associated with assets held for sale	23	-	(3)
Advances from affiliates	420	(4)	(19)

[1] Represents the effect on net income (loss) and other comprehensive income (loss) for the three months ended September 30, 2008.

Capital Management

Our total capital as of September 30, 2008 and December 31, 2007 is calculated as follows:

(Unaudited, in millions)	**September 30, 2008**	December 31, 2007 Restated—Note 1
Short and long-term debt	$ **301**	$ 245
Non-controlling interest in subsidiary	**6**	6
Shareholders' equity[1]	**684**	1,099
	991	1,350
Less: cash and cash equivalents	**(5)**	(14)
Total capital	$ **986**	$ 1,336

[1] Shareholders' equity includes accumulated other comprehensive loss.

Our objectives when managing capital are:

- to make proper capital investments for asset compliance and maintenance purposes to ensure that we remain competitive and in compliance with regulatory requirements;

- to make proper capital investments to seek opportunities to reduce costs and to increase sales of higher-margin grades of coated and value-added specialty papers; and

- from a financial perspective, to achieve stable liquidity and to reduce our debt levels.

Our primary sources of liquidity and capital resources are cash on hand and available borrowings under our credit facility. Our major cash requirements are to fund operating activities, including changes in working capital, capital expenditures and debt service obligations.