

Closing Keynote – Frank A. Dottori, President & CEO, Tembec

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Ladies and Gentlemen:

I was asked to make some comments on how Pulp and Paper professionals can best attain successful outcomes in today's shifting market place and business culture.

Well, I am not sure I have the solution judging from the financial performance of my company recently.

Let me begin by telling you a little bit about Tembec. I believe the experience and principles are applicable to the industry. As noted in the introduction Tembec was created in 1973 by reviving a shutdown mill in North Western Quebec. The shutdown was emotionally and economically devastating, as it was the only major industrial employer in this region. Approximately 1500 regional jobs were eliminated under a 90-day notice.

It was a crisis situation. The community, employees and local management reacted by taking the initiative to help themselves and control their own destiny. (For those of you who are interested about the social issues, you can get a copy of the National Film Board docufilm "A Town That Won't Die").

The situation was the basis for Tembec's Vision: "A Company of people building their own future".

We then developed a Mission Statement, which outlined what we wanted to do.

We followed this with a set of principles and guidelines to help us achieve our mission.

We set high-level 5-year goals and objectives, which are continually reviewed and updated. (All this information is available on our web site or Annual Reports).

We make employees accountable for meeting the goals and we reward them accordingly via profit sharing programs, share purchase programs and good salaries.

We try to create an environment where employees can participate, be creative, be constructively critical without fear of retaliation by their superiors.

In essence, we try to adhere and share the Vision of "A Company of people building their own future" with all employees of the company regardless of position.

We are old fashioned. We try to protect our employees and provide them with job security. In return, we want commitment and loyalty.

Has our formula been successful?

These are the facts and you can come to your own conclusion.

In 1973 we started out with:

- 350 employees
- Sales of \$35 Million
- Assets \$2.5 Million at one site

Today in 2003 we have:

- Over 10,000 employees
- Assets of \$4.0 Billion Canadian
- Sales over \$4.0 Billion Canadian
- 55 sites across Canada, U.S. France and Chile
- 3rd largest Forest Products company in Canada and 12th in North America and 45th on the global scale

and we are still growing with our objective of doubling over the next 5 years.

- We have established Tembec as a leader in Forest Environmental Responsibility with our Forever Green EMP.
- Played key role in Living Legacy agreement in Ontario with WWF and other ENGO's.
- Recently certified 5.0 Million Acres under FSC certification and will do more.
- Support Kyoto Protocol and committed to eliminating fossil fuels by 2010.

In Canada, we have established ourselves as one of the most socially responsible companies with our Education Fund, our Environment Fund and Community Fund which give donations to improving the quality of life in the communities where we operate. We also have Regional Advisory Committees that issue reports to our Board of Directors on regional issues.

Where do we want to go?

We want to continue our culture of social and environmental and ethical leadership. We want to continue to grow our company and our industry. We want to maintain our culture of Entrepreneurship and Innovation. We believe that along with this industry we have a future.

Forest Products is not a Sunset industry. We are an evergreen industry built on a natural environmentally friendly resource. This industry came to being with mankind and will be here forever. It is based on the carbon cycle.

The problem we have is that many industry leaders, governments and the public do not recognize this fact anymore. We have become depressed. We seem resigned to failure.

After ten to fifteen years of persecution by environmentalists and financial analysts this is understandable but not acceptable.

A few years back the steel industry attacked the forest products industry via commercials that you probably recall. Steel, the only house standing after a hurricane. Wood homes left a gaping hole in a pristine forest vs steel homes made from old recycled cars. What did our industry do? Nothing. I believe we should have countered with ads showing an electrical storm with fierce lightning and two houses, one made from wood and one from steel with a caption, "Which house would you like to be in or feel comfortable in"?

It is time to stop being depressed. It is time to get aggressive and fight back.

Let's look at the facts. I will speak mostly with respect to the Canadian industry but I believe the same is true in the US. In the environmental area since 1990 the industry has accomplished the following:

- Dioxins - elimination of the issue during the 1990's in spite of the fact industry contributed only 2% of the problem. Has agriculture, the chemical industry or the public done anything similar?
- Water - 94% reduction in BOD
95% reduction in Suspended Solids
- Green House Gas - approximately 25% reduction. Already meeting Kyoto targets.
- Forest Certification - Most companies are ISO 14000 certified and there is an industry commitment to be 3rd party certified by 2005 (SFI, CSA or FSC).
- Sustainability/Biodiversity - full commitment by industry and governments.

We have cleaned up our act! Let others do the same.

On the Financial Front

- The North American industry has consolidated and rationalized facilities better than any other industry.
- Our relative financial performance has been better than most high tech and industrial sectors.
- We suffer from less over-capacity than steel, fibre optics, microchips, airlines, agriculture and on and on. Some have 50 to 200% over-capacity; we have about 5 to 10%.
- We have less volatility - but momentum players don't like this. They like volatile pure plays. Do they really care about our industry? Analysts talk about shareholder value but does it really matter if you churn shares as most investors do? Is it buy low, sell high and who cares about next year? They care about share price not value and although related the two are not necessarily the same at any given point in time. Creation of value takes time. Perception of value is short-term.
- Our future should be bright going forward but we need strong aggressive leadership. Our industry can create value if we exhibit a lot more discipline going forward.

Our industry needs to set out

- A Vision
- Goals and Objectives
- A Plan to make it happen
- We need to sell and promote our industry

We tend to focus too much on globalization, consolidation and on the next quarter's results. Our vision seems to be "try to satisfy the analysts, get the share prices up, cash out your options and move on".

There is no doubt that the primary purpose of business is to make money and get a return on the capital invested. Our problem is that we have too much capital invested and our returns are too low.

This industry has not done well over the last 20 years if we look at either share prices or value creation. Most companies have gained little over 20 years on average. Our returns are not much better than US 10-year treasuries but carry more risk.

We need to earn 10 to 15% on our capital employed to become the darlings of the investment community.

The Pulp and Paper sector in particular is too capital intensive generating only 50 to 75 cents per dollar of invested capital. One of the worst of all industries. We need to improve our turnover ratio and get more dollars of revenue per dollar invested. We can do this by reducing Capex per unit or improving the margins per unit. How do we do this? Let me ask a few questions and think about the answers.

- Are we focusing enough on new technologies, which will lower capital costs per dollar? Maybe we should build minimills instead of monster mills that disrupt the market and cost a billion dollars.
- Are we investing 3% to 5% in R&D and new products? Are we supporting R&D institutes and universities? or are we closing down our R&D facilities and reducing expenditures to improve quarterly results. Is the short-term gain worth the long-term pain? Our industry will fail if we don't innovate and develop new processes and products.
- Are we promoting our industry as a high tech industry encouraging the brightest scientists and engineers to join this great industry? Are we raising the technical and hiring standards of our employees and training them to cope with the new technologies and challenges to develop new ideas, to be creative and make this an innovation industry. How many of you have embedded university hiring programs to train and evaluate new scientists and engineers? How do we compare with the oil, high tech or plastics industry?
- Do we have major programs for reforestation, development of fast growing species or will we all go to Brazil?
- Are we looking to grow the North American markets for Forest Products or are we trying to decimate each other via illogical defensive actions.

Look at the Softwood Lumber issue. Hundreds of millions of dollars wasted on artificial legal arguments over the past 20 years instead of using the monies constructively to grow demand and inventing new products.

Would we have a problem if these \$ were spent:

- Promoting wood consumption. The US uses 0.44 m³/person/year, Canada 0.50 m³/person/year, Finland 1.00 m³/person/year. A 10% increase in US consumption would eliminate the over supply.
- Developing new products to displace cement, steel, plastics and those other non-friendly products that contribute to air pollution and Green House Gases.

- Some investors believe we are stupid and this dispute and waste of money is indicative of industry leadership.

I could go on for sometime and I am sure most of you could generate a long list of your own as well.

The crisis is here! We need strong leadership!

As an industry, we need a Vision, a Mission, a set of Principles and Goals for this industry. Our forest products associations like the AF&PA, FPAC and PIMA need to take this leadership role with CEO's support. We need to get our act together and focus on growing our business.

In Canada we are in the process of doing this by creating a Forest Sector Innovation Council. It will set 5 to 10 years vision for the industry along with specific goals and an organization to focus on getting results.

But to succeed, we need commitment by CEO's and their corporations. This is not readily evident as yet.

We need to spend less dollars on Fixed Asset and Capital and more on Intellectual Capital if we are to generate more \$ of sales per dollar of capital invested and in turn improve our financial results.

If we do not have customers, we do not need a business. We need to invest in developing new products to service our customers better, grow our sales and increase our margins. This leads to better financial results and investor confidence for the future.

To achieve this we need to stimulate creativity and innovation. We must get more from less. This can only come from most creative and motivated employees. We need people power

Creativity does not need an IQ of 150 plus. Anyone can do it in the right nurturing environment. Creativity can be as simple as rearranging existing facts - e.g. fruit cocktail. No need to invent a fruit cocktail tree, just mix existing fruit and create a new product.

Our major strategic capital investments are justified over five, ten, fifteen years yet we worry about the next quarter results.

As noted earlier we need to take a longer view of our business. We all talk about shareholder value but most investors today are momentum players. We need to focus on long-term creation of wealth and value added and stop catering to these short-term promoters that sell and buy on perception/momentum.

We must make a serious commitment to improving the Intellectual Capital of our industry - people. We invest \$100K on a capital item but won't invest \$100K on a good engineer that can bring a 100%+ ROI every year.

Our industry has seen a massive cutback in R&D in recent years. We cannot continue to reduce R&D investment as well as our support for universities and research institutes. Successful industries invest at levels 2 or 3 times higher than our industry. Let's take a long hard pause here and think of the consequences. Think of P&G and their focus on new products, consumers and people. It works.

If we do not focus on the future potential and develop new and better products we'd better watch out that we are not taken over by the soybean industry. I think that industry spends more dollars on R&D than we do.

We need to move from being a hewer of wood and drawer of water to a supplier of environmentally friendly high tech consumer products. The future can be ours but we need to focus on attracting highly skilled people.

This industry has been here since the beginning of mankind and will continue until the end of mankind. It is a Forever Green industry. It's time for all of us to look to the future and think of the possibilities and potential.

In the end it's people that make the difference not equipment. Let's focus on making our people the brightest and best trained and the most creative and our industry will prosper. Think of what this industry could do if young engineers and scientists made it their preferred career choice. It is up to us to make it happen.

Who knows perhaps?

Profitability = Intellectual Capital?

i.e. $P = 1C^2$

or Enterprise Value = money x creativity²

i.e. $E = mc^2$

Let's not be short sighted and miss the opportunity.

We can build our own future