Management's Discussion and Analysis

August 13, 2014

This management's discussion and analysis ("MD&A") has been prepared by Hardwoods Distribution Inc. ("HDI" or the "Company") as of August 13, 2014. This MD&A covers our unaudited interim condensed consolidated financial statements as at and for the three and six month periods ended June 30, 2014 ("Interim Financial Statements"). As well, it provides an update to the MD&A section contained in our 2013 Annual Report. The information below should be read in conjunction with our Interim Financial Statements and the audited consolidated financial statements and accompanying notes for the years ended December 31, 2013 and 2012 ("Audited Financial Statements"). Results are reported in Canadian dollars unless otherwise stated, and have been prepared in accordance with International Accounting Standards ("IAS") 34, "Interim Financial Reporting" as permitted by International Financial Reporting Standards ("IFRS"). For additional information, readers should also refer to our Annual Information Form and other information filed on www.sedar.com.

In this MD&A, references to "EBITDA" are to earnings before interest, income taxes, depreciation and amortization, where interest is defined as net finance costs as per the consolidated statement of comprehensive income. In addition to profit or loss, we consider EBITDA to be a useful supplemental measure of a company's ability to meet debt service and capital expenditure requirements, and we interpret trends in EBITDA as an indicator of relative operating performance.

EBITDA is not an earnings measure recognized by IFRS and does not have a standardized meaning prescribed by IFRS. Investors are cautioned that EBITDA should not replace profit or loss or cash flows (as determined in accordance with IFRS) as an indicator of our performance. Our method of calculating EBITDA may differ from the methods used by other issuers. Therefore, our EBITDA may not be comparable to similar measures presented by other issuers. For reconciliation between EBITDA and profit or loss as determined in accordance with IFRS, please refer to the discussion of Results of Operations described in section 3.0 of this report.

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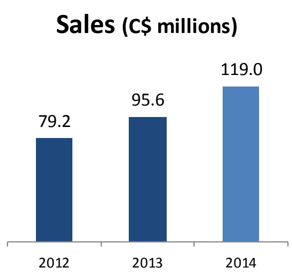
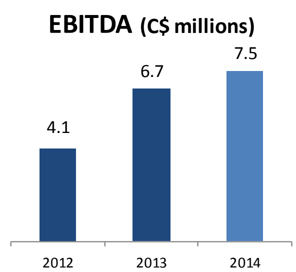
1.0 Executive Summary

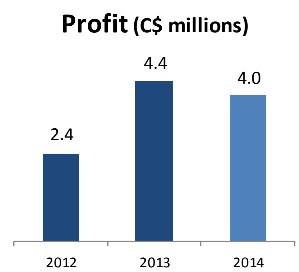
1.1 Overview

We achieved the best quarterly sales results in our history and generated near-record EBITDA in the three months ended June 30, 2014. Second quarter revenue climbed 24.5% to $119.0 million and EBITDA increased 11.9% to $7.5 million, compared to the same period in 2013. This was our strongest quarterly EBITDA performance in 10 years. Profit for the period was $4.0 million, down slightly from $4.4 million a year ago, primarily reflecting higher US corporate taxes as well as a decrease in foreign exchange gains between the periods.

Three Months Ended June 30th:

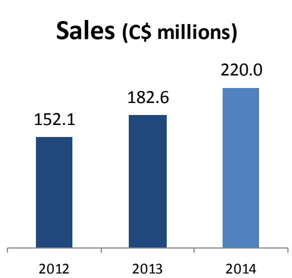


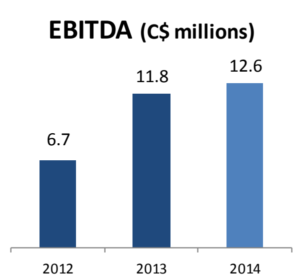


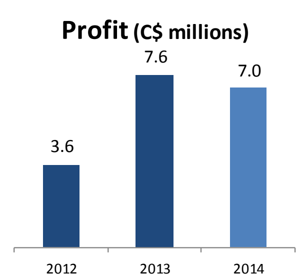


Results were also strong in the six months ended June 30, 2014, with sales up 20.5% to $220.0 million and EBITDA rising 6.4% to $12.6 million. We recorded first half 2014 profit of $7.0 million.

Six Months Ended June 30th:







Organic and acquisition-based growth contributed to the strong sales performance in both the second quarter and first half 2014 periods, supported by continued improvement in the US housing market. According to the US Census Bureau, the seasonally adjusted annual rate of US housing starts averaged 980,333 starts during the second quarter, up 13.4% from 864,667 in the same period last year.

Sales results also benefitted from a year-over-year decline in the value of the Canadian dollar relative to the US dollar. A weaker Canadian dollar benefits us by: i) increasing the value of sales and profits earned in our US operations when translated into Canadian dollars for financial reporting purposes; ii) increasing the selling price of US dollar-denominated products sold to our Canadian customers; and iii) improving the export competitiveness of our Canadian industrial customers, many of whom have the capability to sell their manufactured products in the US.

Product pricing was mixed for the second quarter, with hardwood lumber prices higher and domestic panel prices remaining generally stable compared to the same time a year ago. Prices for some of our import products were weaker year-over-year, reflecting the impact of preliminary duties of 22% that were added to the price of Chinese plywood imports in the second quarter of 2013 due to a trade dispute in the US. These duties did not apply in the current period because the trade case was dismissed in the fourth quarter of 2013.

As anticipated, second quarter and first half gross profit margin did not match the unusually high results achieved last year during a period of rapid product price escalation. At 17.2% and 17.6% respectively, gross margins in the three and six month 2014 periods reflect more stable product pricing, increased competition, and strategic efforts to increase market share in certain parts of the business. Second quarter margin also reflects the addition of the Hardwoods of Michigan Inc. ("HMI") business, which we acquired on April 28, 2014.

Based in Clinton, Michigan, HMI is a fully integrated producer and exporter of high quality hardwood lumber and is expected to generate approximately $33 million in additional revenues annually, with opportunity to grow. HMI provides cross-selling opportunities for our established lines of import products and expands upon our value-added manufacturing capabilities. HMI is a strong and strategic addition to the business, well-timed to the ongoing recovery in the US housing market. In conjunction with the HMI transaction, we increased our US credit facility from US$50.0 million to US$79.1 million and extended the term of the facility to April 27, 2017.

We were successful in increasing cash provided by operating activities by $12.0 million during the second quarter, compared to the same period in the prior year. This increase in operating cash flow came primarily through more efficient management of working capital, and allowed us to finance a substantial portion of the HMI acquisition with internally generated cash flow while maintaining a strong balance sheet to support our future growth initiatives.

Our EBITDA results were strong in both the second quarter and first half periods and contributed to healthy EBITDA as a percentage of sales margins of 6.3% and 5.7% respectively. Profit was slightly lower year-over-year due to higher depreciation and lower foreign exchange gains, both of which are non-cash items. Income taxes were also higher reflecting higher taxable income generated in the United States, where corporate tax rates are higher than in Canada.

Overall, our second quarter and first half financial results were strong and reflect favourable market conditions and the positive impact of our business strategies. Based on this performance, our Board of Directors approved a quarterly dividend of $0.045 per share, payable on October 31, 2014 to shareholders of record as at October 20, 2014.

1.2 Outlook

We anticipate continued year-over-year sales growth through the second half of 2014 supported by the continued US market recovery, implementation of our business strategies, the positive foreign exchange impact of a weaker Canadian dollar, and the addition of the HMI business, partially offset by a recent softening trend in prices for some hardwoods lumber species.

The National Association of Homebuilders is calling for 1.038 million new housing starts in 2014, somewhat lower than previous estimates, but still up 12.3% over 2013. Renovation spending in the US is expected to rise 6.5% year over year according to the Home Improvement Research Institute, and non-residential construction is expected to increase 11.6% according to McGraw Hill Construction estimates.

In the Canadian market, 2014 housing starts are expected to remain unchanged from 2013 levels, while growth in the renovation and commercial construction markets is expected to be in line with inflation.

Our focus in the second half of 2014 will be on continuing to expand our US market share and successfully integrating our newly acquired HMI business. We are also actively pursuing our “Leverage Imports” and “Strengthen Commercial” strategies which focus on:

- Growing sales of our high-quality proprietary import lines, supported both by the established quality assurance team located in Asia and new international sourcing initiatives designed to bring world-wide product solutions to Hardwoods’ customers.

- Capitalizing on significant opportunities in the commercial market. In particular, we are actively growing our supply of first-tier products for commercial customers and capitalizing on our import capabilities to offer off-shore product solutions to the commercial sector to supplement domestic product solutions.

Going forward, we have a strong and experienced management team in place to run the business and execute our strategy while CEO Lance Blanco recovers from a cycling accident that occurred in late July. The Board has appointed Rob Brown, Hardwoods' current Chief Financial Officer, as acting Chief Executive Officer until Mr. Blanco can resume his duties, and other senior executives have assumed expanded roles.

The Board of Directors will continue to review our financial performance and assess quarterly dividend payments on a regular basis. However in terms of cash utilization, our primary focus through the balance of 2014 will remain on retaining the cash necessary to finance the significant market opportunity in the US and keeping our balance sheet strong to support strategic acquisitions.

2.0 Background

2.1 Company Overview

Hardwoods Distribution Inc. is a publicly traded company that holds, indirectly, a 100% ownership interest in Hardwoods Specialty Products LP and Hardwoods Specialty Products US LP (collectively, "Hardwoods" or the "Business"). Hardwoods Distribution Inc. is listed on the Toronto Stock Exchange and trades under the symbol HWD.

2.2 Business and Industry Overview

Serving customers for over 50 years, Hardwoods is one of North America's largest distributors of high-grade hardwood lumber and specialty sheet goods to the cabinet, moulding, millwork, furniture and specialty wood products industries. At June 30, 2014 we operated 33 facilities located in 17 states and 5 provinces throughout North America. Five of these facilities include light manufacturing capabilities to create customer moulding and millwork packages for our customers, and one facility (HMI) is a fully integrated producer and exporter of high-quality, value-added hardwood lumber. To maximize inventory management, we utilize a hub and spoke distribution system, with major hub distribution centres holding the bulk of our inventory and making regular truck transfers to replenish stock in satellite distribution centres that are located in smaller markets.

Approximately 55% of our sales are made up of hardwood plywood and non-structural sheet goods such as medium-density fiberboard, particleboard and melamine-coated stock. Approximately 37% of our sales are of high-grade hardwood lumber. Our sheet goods and lumber are complementary product lines; both are key products used by our customers in the manufacture of their end-use products. The balance of our product sales, about 8%, is made up of other specialty products.

Our distribution locations provide the critical link between mills that manufacture large volumes of hardwood lumber and sheet goods, and industrial customers that require smaller quantities of many different hardwood products for their own manufacturing processes. Our distribution centres provide a means for hundreds of hardwood mills to get their product to thousands of small-to-mid-sized industrial manufacturers. We add value to our suppliers by buying their product in volume and paying them promptly, effectively acting as their third-party sales force. We add value for our customers by providing them with the materials they need on a just-in-time basis, remanufacturing materials to customer specifications where required, selling in smaller quantities and offering a wider range of product selection than the customer would be able to purchase directly from an individual mill. We also provide an important source of financing for our customers by allowing them to buy material from us on approved credit.

Our customer base manufactures a range of end-use products, such as cabinetry, furniture and custom millwork. These products in turn are sold into multiple sectors of the economy, including new home construction, renovation, non-residential construction and institutional markets. As a result of this diversity, it is difficult to determine with certainty what proportion of our products ends up in each sector of the economy. We estimate about 60% of our products are used in new residential construction, in the form of cabinets, mouldings, custom finishing, and home furniture. We believe the balance of our products end up in other sectors of the economy not associated with new residential construction, such as home renovations, finishing millwork for office buildings, restaurant and bar interiors, hotel lobbies, retail point-of-purchase displays, schools, hospitals, custom motor coaches, yacht interiors and other specialty areas.

The majority of the hardwood lumber distributed in North America is harvested from North American hardwood forests, located principally in the Eastern United States, and is milled by hundreds of small mills. Imported hardwood lumber is largely limited to specialty species that generally do not compete with domestic hardwood lumber. Sheet goods are generally produced in North America by large manufacturers using domestic hardwoods and other materials, although imported hardwood plywood volumes have been increasing. Both domestic and imported hardwood lumber and plywood are distributed principally by third parties such as us.

3.0 Results of Operations

3.1Three Months Ended June 30, 2014 and June 30, 2013

Selected Unaudited Consolidated Financial Information (in thousands of Canadian dollars)						
		For the three months Ended June 30 2014		For the three months Ended June 30 2013	$ Increase (Decrease)	% Increase (Decrease)
Total sales	$	119,038	$	95,617	$ 23,421	24.5%
Sales in the US (US$)		*83,521*		*69,535*	*13,986*	20.1%
Sales in Canada		*27,904*		*24,484*	*3,420*	14.0%
Gross profit		20,528		18,081	2,447	13.5%
Gross profit %		*17.2%*		*18.9%*		
Operating expenses		(13,500)		(11,683)	1,817	15.6%
Profit from operating activities		7,028		6,398	630	9.8%
Add: Depreciation and amortization		515		342	173	50.6%
Earnings before interest, taxes, depreciation and amortization ("EBITDA")	$	7,543	$	6,740	$ 803	11.9%
Add (deduct):						
Depreciation and amortization		(515)		(342)	(173)	-50.6%
Net finance income (cost)		(414)		102	(516)	-505.9%
Income tax expense		(2,618)		(2,097)	(521)	-24.8%
Profit for the period	$	3,996	$	4,403	$ (407)	-9.2%
Basic and fully diluted profit per share	$	0.24	$	0.27		
Average Canadian dollar exchange rate for one US dollar		1.090		1.023		

Sales

For the three months ended June 30, 2014, total sales increased 24.5% to $119.0 million, from $95.6 million during the same period in 2013. Of this $23.4 million year-over-year increase, $17.7 million was due to stronger underlying sales and $5.7 million reflects the positive impact of a weaker Canadian dollar when translating our US sales to Canadian dollars for reporting purposes.

Sales from our US operations, which comprise approximately three quarters of our revenues, increased by US$14.0 million, or 20.1%, to US$83.5 million, from US$69.5 million in the same period in 2013. Organic growth accounted for over half of this improvement, with sales increasing by US$7.3 million, or 10.5% as a result of stronger underlying sales activity and higher pricing on some product lines. Acquisitions, including the HMI business acquired on April 28, 2014 and the Leland import lumber business acquired on May 31, 2013, contributed US$6.7 million or 9.6% to the increase in US sales.

Sales in Canada, which comprise approximately one quarter of our revenues, increased by $3.4 million, or 14.0%, year-over-year. Double-digit growth was achieved in all regions, reflecting successes in winning new business, as well as overall stronger product prices and the positive impact of a weaker Canadian dollar as described in Section 1.1.

Gross Profit

Gross profit for the three months ended June 30, 2014 increased 13.5 % to $20.5 million, from $18.1 million in the second quarter of 2014. This $2.4 million improvement reflects the higher sales for the period, partially offset by a lower gross profit margin. As a percentage of sales, second quarter gross profit margin was 17.2%, compared to 18.9% last year. The unusually strong gross profit margin in the second quarter of 2013 was achieved at a time when prices for hardwood plywood products were increasing rapidly due to the imposition of preliminary duties against Chinese plywood imported into the US. That trade case was eventually dismissed in November of 2013, but caused unusual variation in panel pricing and therefore margins, during the second quarter of 2013. Gross profit margin of 17.2% in the second quarter of 2014 period was below our historic margin target of around 18%, reflecting competitive conditions, as well as the impact of the acquired HMI manufacturing business which generates a slightly lower gross profit percentage than does Hardwoods' traditional distribution business.

Operating Expenses

Operating expenses increased to $13.5 million in the second quarter of 2014, from $11.7 million during the same period last year. The $1.8 million increase reflects $0.6 million in incremental costs from the acquired HMI and Leland businesses, $0.7 million in higher costs incurred to support existing and anticipated sales growth, and $0.5 million of higher expense due to the impact of a weaker Canadian dollar on translation of US operating expenses. As a percentage of sales, operating expenses were 11.3% of sales in the three months ended June 30, 2014, compared to 12.2% during the same period in 2013.

EBITDA

We generated EBITDA of $7.5 million in the second quarter of 2014, an increase of $0.8 million or 11.9%, from $6.7 million in the same period last year. This primarily reflects the $2.4 million increase in gross profit, partially offset by the $1.8 million increase in operating expense before depreciation.

Net Finance Income (Cost)

(in thousands of Canadian dollars)		Three months ended June 30, 2014		Three months ended June 30, 2013		$ Increase (Decrease)
Finance expense:						
Interest on bank indebtedness	$	(319)	$	(265)	$	54
Accretion of finance lease obligation		(27)		(25)		2
Foreign exchange losses		(184)		-		184
Total finance expense		(530)		(290)		240
Finance income:						
Interest on trade receivables,						
customer notes, and employee loans		116		138		(22)
Foreign exchange gain		-		254		(254)
Total finance income		116		392		(276)
Net finance income (cost)	$	(414)	$	102	$	516

Second quarter net finance cost was $0.4 million, compared to a net finance income of $0.1 million during the same period in 2013. As shown in the preceding table, the main factor in this increase was a change in foreign exchange gain/losses between the periods. This primarily reflects the impact of changes in the Canadian/US dollar exchange rate on translation for reporting purposes of intercompany debt held by or with subsidiaries of the Company. During the three months ended June 30, 2014, a strengthening of the Canadian dollar resulted in a foreign exchange loss of $0.2 million on this intercompany debt, compared to a weakening of the Canadian dollar and a corresponding $0.3 million foreign exchange gain in the comparative period in 2013.

Income Tax Expense

Income tax expense increased to $2.6 million in the second quarter of 2014, from $2.1 million in the same period in 2013. This increase primarily reflects higher taxable income generated in the US, where corporate tax rates are higher than in Canada.

Profit for the Period

Profit for the three months ended June 30, 2014 was $4.0 million, compared to $4.4 million during the same period in 2013. The $0.4 million decrease in profit reflects a $0.2 million increase in depreciation and amortization, a $0.5 million increase in net finance cost, and the $0.5 million increase in income tax expense, partially offset by the $0.8 million improvement in EBITDA.

3.2 Six Months Ended June 30, 2014 and June 30, 2013

Selected Unaudited Consolidated Financial Information (in thousands of Canadian dollars)	For the six months Ended June 30 2014	For the six months Ended June 30 2013	$ Increase (Decrease)	% Increase (Decrease)
Total sales	$ 219,972	$ 182,600	$ 37,372	20.5%
Sales in the US (US$)	*153,062*	*133,447*	*19,615*	14.7%
Sales in Canada	*52,093*	*47,044*	*5,049*	10.7%
Gross profit	38,791	33,981	4,810	14.2%
Gross profit %	*17.6%*	*18.6%*		
Operating expenses	(27,098)	(22,769)	4,329	19.0%
Profit from operating activities	11,693	11,212	481	4.3%
Add: Depreciation and amortization	953	671	282	42.0%
Earnings before interest, taxes, depreciation and amortization ("EBITDA")	$ 12,646	$ 11,883	$ 763	6.4%
Add (deduct):				
Depreciation and amortization	(953)	(671)	(282)	-42.0%
Net finance income (cost)	(349)	269	(618)	229.7%
Income tax expense	(4,383)	(3,898)	(485)	-12.4%
Profit for the period	$ 6,961	$ 7,583	$ (622)	-8.2%
Basic and fully diluted profit per share	$ 0.42	$ 0.46		
Average Canadian dollar exchange rate for one US dollar	1.097	1.016		

Sales

For the six months ended June 30, 2014 total sales increased to $220.0 million, from $182.6 million in the first half of 2013, an increase of $37.4 million or 20.5%. Higher underlying sales accounted for $25.0 million of the sales growth, while $12.4 million reflects the positive impact of a weaker Canadian dollar when translating our US sales to Canadian dollars for reporting purposes.

Sales in our US operations increased by US$19.6 million, or 14.7% in the first half of 2014 compared to the same period in the prior year. Incremental revenue from acquired businesses provided sales of US$7.7 million or 5.8% sales growth. The remaining US$11.9 million increase in sales came from existing operations, representing an organic growth rate of 8.9% year-over-year. In Canada, first half sales increased by $5.0 million compared to the same period in 2013, providing an organic growth rate of 10.7% year-over-year.

Gross Profit

First-half gross profit increased to $38.8 million, from $34.0 million in the first six months of 2013. The 14.2% improvement reflects increased sales, partially offset by a lower gross profit margin. As a percentage of sales, gross profit decreased to 17.6% in the first half of 2014, from 18.6% during the same period in 2013. As described previously, gross profit margin in the first six months of 2013 was unusually strong, aided by a rapid increase in Chinese import panel prices as the result of a trade action against the product in the US at that time. The trade action was later dismissed.

Operating Expenses

Operating expenses increased $4.3 million to $27.1 million in the first six months of 2014, from $22.8 million during the same period in 2013. The increase reflects $2.4 million in higher costs incurred to support growth, $1.3 million of higher expense due to the impact of a weaker Canadian dollar on translation of US operating expenses, and $0.6 million in incremental costs from the acquired HMI and Leland businesses. As a percentage of sales, first-half operating expenses improved to 12.3% of sales, from 12.5% in 2013.

Depreciation and Amortization

Depreciation and amortization for the first half of 2014 was $1.0 million, compared to $0.7 million in the same period in 2013. The $0.3 million increase reflects depreciation associated with additional property, plant and equipment investments made in the business including the assets from the acquired HMI manufacturing business.

EBITDA

For the six months ended June 30, 2014, EBITDA increased to $12.6 million, from $11.9 million during the same period in 2013. The $0.7 million improvement reflects the $4.8 million increase in gross profit, partially offset by a $4.1 million increase in operating expenses, net of depreciation and amortization.

Net Finance Income (Cost)

(in thousands of Canadian dollars)		**Six months ended June 30, 2014**		**Six months ended June 30, 2013**		**$ Increase (Decrease)**
Finance expense:						
Interest on bank indebtedness	$	(538)	$	(478)	$	60
Accretion of finance lease obligation		(53)		(44)		9
Total finance expense		(591)		(522)		69
Finance income:						
Interest on trade receivables customer notes, and employee loans		220		241		(21)
Foreign exchange gain		22		550		(528)
Total finance income		242		791		(549)
Net finance income (cost)	$	(349)	$	269	$	618

Net finance cost during the first half of 2014 was $0.3 million, compared to a net finance income of $0.3 million during the same period in 2013. As shown in the preceding table, the main factor in this increase was a $0.5 million decrease in foreign exchange gain between the periods. This primarily reflects the impact of changes in the Canadian/US dollar exchange rate on translation for reporting purposes of intercompany debt held by or with subsidiaries of the Company. During the six months ended June 30, 2013, a weakening of the Canadian dollar resulted in a foreign exchange gain of $0.6 million on this intercompany debt, compared to just $22,000 in the same period in the current year.

Income Tax Expense

Income tax expense increased to $4.4 million in the first six months of 2014, from $3.9 million in the same period in 2013. This increase primarily reflects higher taxable income generated in the US, where corporate tax rates are higher than in Canada.

Profit for the Period

For the six months ended June 30, 2014, we generated profit of $7.0 million, compared to $7.6 million during the same period in 2013. The $0.6 million decrease reflects a $0.3 million increase in depreciation and amortization, a $0.6 million increase in net finance cost, and a $0.5 million increase in income tax expense, partially offset by the $0.8 million improvement in EBITDA.

4.0 Quarterly Financial Information and Seasonality

(in thousands of dollars)	Q2 2014	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012	Q3 2012
Total sales	$ 119,038	$ 100,934	$ 91,069	$ 97,546	$ 95,617	$ 86,983	$ 74,133	$ 79,862
Profit	3,996	2,965	2,375	3,109	4,403	3,180	1,313	1,264
Basic profit per share or unit	0.24	0.18	0.14	0.19	0.27	0.19	0.08	0.08
Fully diluted profit per share or unit	0.24	0.18	0.14	0.19	0.27	0.19	0.08	0.08
EBITDA	7,543	5,103	4,216	5,269	6,740	5,143	2,407	3,313

The preceding table provides selected quarterly financial information for our eight most recently completed fiscal quarters. This information is unaudited, but reflects all adjustments of a normal, recurring nature which are, in our opinion, necessary to present a fair statement of the results of operations for the periods presented. Quarter-to-quarter comparisons of our financial results are not necessarily meaningful and should not be relied upon as an indication of future performance. Historically, the first and fourth quarters have been seasonally slower periods for our business. Net earnings reported in each quarter may be impacted by changes to the foreign exchange rate of the Canadian and US dollar (including changes in foreign exchange gains/losses arising on translation of intercompany debt), as well as by acquisitions, such as our second quarter 2013 acquisition of the import lumber business acquisition in Leland, NC, and our second quarter 2014 acquisition of HMI.

5.0 Liquidity and Capital Resources

5.1 Cash Flows from Operating, Investing and Financing Activities

Selected Unaudited Consolidated Financial Information (in thousands of Canadian dollars)	**Three months ended June 30**			**Six months ended June 30**		
	2014	**2013**	**$ Change**	**2014**	**2013**	**$ Change**
Cash provided by operating activities before changes in non-cash working capital	$ 5,796	$ 5,224	$ 572	$ 9,709	$ 9,738	$ (29)
Changes in non-cash working capital	383	(11,005)	11,388	(11,279)	(24,942)	13,663
Net cash provided by (used in) operating activities	6,179	(5,781)	11,960	(1,570)	(15,204)	13,634
Net cash used in investing activities	(15,466)	(3,164)	(12,302)	(15,685)	(3,084)	(12,601)
Net cash provided by financing activities	9,284	8,934	350	17,198	18,205	(1,007)
Increase (decrease) in cash	(3)	(11)	8	(57)	(83)	26
Cash, beginning of period	24	22	2	78	94	(16)
Cash, end of period	$ 21	$ 11	$ 10	$ 21	$ 11	$ 10

In the three months ended June 30, 2014, cash provided by operating activities increased to $6.2 million. This compares to cash used in operating activities of $5.8 million during the same period in 2013. Cash provided by operating activities, before changes in non-cash working capital, increased by $0.6 million. This primarily reflects the $0.8 million increase in second quarter EBITDA. Investment in non-cash working capital was $11.4 million lower in the second quarter of 2014 compared to the same period in the prior year primarily reflecting more efficient utilization of inventory and accounts receivable. An analysis of changes in working capital is provided in section 5.2 of this report.

For the six months ended June 30, 2014, cash used in operating activities was $1.6 million, compared to $15.2 million during the same period in 2013. Cash provided by operating activities, before changes in non-cash working capital, was essentially unchanged with the $0.8 million increase in EBITDA offset by a $1.0 million increase in income taxes paid. First half investment in non-cash working capital decreased by $13.7 million compared to the same period in 2013. An analysis of changes in working capital is provided in section 5.2 of this report.

Net cash provided by (used in) investing activities

Net cash used in investing activities increased by $12.3 million and $12.6 million, respectively, in the second quarter and first six months of 2014, compared to the same periods in 2013. The increase in both periods primarily reflects an increase in cash paid for business acquisitions. In the second quarter of 2014, cash paid in the HMI acquisition was $15.3 million. By comparison, we completed the Leland acquisition for $3.0 million during the same period in 2013. Net cash provided by (used in) investing activities comprises cash collections on long-term receivables and proceeds from disposal of property, plant and equipment, less expenditures made on business acquisitions as well as capital expenditures made to acquire additional property, plant and equipment.

Capital expenditures in our traditional distribution business have been low as we lease our buildings and contract out all freight delivery services. Capital expenditures in this part of our business are principally for the replacement of forklifts, furniture and fixtures, leasehold improvements and computer equipment.

Our Paxton business, which includes five branches, requires some additional ongoing investment in moulders and other light remanufacturing equipment. Paxton also buys trailers and leases tractor units for use in delivery of product to customers, whereas other Hardwoods operations contract out this freight delivery service to third-party carriers.

We believe we have made sufficient expenditures to sustain productive capacity of our business as it relates to our needs for property, plant and equipment.

Our acquisition of HMI on April 28, 2014 will increase our future capital expenditure needs. The HMI business requires ongoing investment in machinery and equipment. We anticipate that additional annual capital expenditure requirements of approximately $0.6 million will be required to maintain the productive capacity of this business.

We also lease automobiles for the use of outside sales representatives and certain managers. For the three months ended June 30, 2014, principle payments on automobile finance lease obligation were $0.2 million (2013 - $0.2 million) and for the six months ended June 30, 2014 were $0.4 million (2013 - $0.4 million).

Net cash provided by financing activities

Although our utilization of cash to make acquisitions increased by $12.3 million in the second quarter and first six months of 2014, this increase in cash outflow was substantially offset by increasing the amount of net cash generated from operating activities during the same periods. As a result, net cash needed to be provided by financing activities increased by just $0.4 million in the second quarter and $1.0 million in the first half of 2014 compared to a year ago, despite completing the HMI acquisition and continuing to achieve organic sales growth in our business.

5.2 Working Capital

Our business requires an ongoing investment in working capital, which includes accounts receivable, inventory, and prepaid expenses, partially offset by provisions and short-term credit provided by suppliers in the form of accounts payable and accrued liabilities. We had working capital of $119.2 million as at June 30, 2014, compared to $98.4 million at December 31, 2013 and $112.0 million at June 30, 2013. Most of this increase is attributable to additional working capital acquired as part of the HMI acquisition.

Our investment in working capital fluctuates from quarter-to-quarter based on factors such as seasonal sales demand, strategic purchasing decisions taken by management, and the timing of collections from customers and payments made to our suppliers. Historically the first and fourth quarters are seasonally slower periods for construction activity, resulting in reduced demand for hardwood products. As a result, sales and working capital requirements may be lower in these quarters. A summary of changes in our non-cash operating working capital during the three and six months ended June 30, 2014 and 2013 is provided below.

(in thousands of Canadian dollars) Source (use) of funds	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
Accounts receivable	$ 2,280	$ (3,872)	$ (5,146)	$ (13,397)
Inventory	(2,521)	(7,328)	(8,732)	(12,444)
Prepaid expenses	(560)	(5)	(414)	219
Accounts payable, accrued liabilities and provisions	1,184	200	3,013	680
Decrease (increase) in non-cash operating working capital	$ 383	$ (11,005)	$ (11,279)	$ (24,942)

Continued compliance with financial covenants under our credit facilities is important to ensure that we have adequate financing available to meet our working capital requirements. The terms of our revolving credit facilities are addressed in section 5.3 of this report.

5.3 Revolving Credit Facilities and Debt Management Strategy

Selected Unaudited Consolidated Financial Information (in thousands of dollars)		As at June 30, 2014		As at December 31, 2013
Cash	$	(21)	$	(78)
Bank indebtedness		46,507		27,881
Net Debt		46,486		27,803
Shareholders' equity		96,509		90,683
Total Capitalization	$	142,995	$	118,486
Net debt to total capitalization		32.5%		23.5%
Previous 12 months EBITDA	$	22,131	$	21,368
Net debt to previous 12 months EBITDA		2.1		1.3

We consider our capital to be bank indebtedness (net of cash) and shareholders' equity. As shown above, our net debt balance increased by $18.7 million to $46.5 million at June 30, 2014, from $27.8 million at December 31, 2013. The increase in net debt reflects additional investment in working capital required to support higher sales and the acquisition of HMI. Net debt at June 30, 2014 of $46.5 million is comparable to the net debt at June 30, 2013 of $45.9 million.

Overall net debt compared to total capitalization stood at 32.5% as at June 30, 2014, compared to 23.5% at December 31, 2013. At June 30, 2014 our ratio of net debt-to-EBITDA for the previous 12 months was 2.1 times, compared to 1.3 times at December 31, 2013. Although the debt utilized to finance the acquisition of HMI is fully included in calculating this ratio, notably only the two months of EBITDA contributed by HMI since it was acquired on April 28, 2014 is included in the previous 12 months EBITDA figure. Net debt-to-EBITDA and net debt-to-total capitalization serve as indicators of our financial leverage, however they are not measures prescribed by IFRS and our method of calculating these measures may differ from methods used by other issuers.

We have independent credit facilities in both Canada and the U.S. These facilities may be drawn down to meet short-term financing requirements such as fluctuations in non-cash working capital, and in the case of the Canadian credit facility, to also make capital contributions to our US operating subsidiary. The amount made available under our Canadian and US revolving credit facilities is, from time-to-time, limited to the extent of the value of certain accounts receivable and inventories held by subsidiaries of the Company. Credit facilities also require ongoing compliance with certain credit ratios. A summary of our credit facilities at June 30, 2014 is provided in the following table. In the second quarter of 2014 we amended our US credit facility to extend its term to April 27, 2017 and to increase the maximum borrowings available under the credit facility from US$50 million to US$79.1 million. The revised credit facility is comprised of US$75.0 million available under revolving credit facilities, and US$4.1 million under a term loan that matures April 27, 2017, with monthly payments based on a five-year amortization.. The US credit facility was increased to provide us with additional flexibility to borrow against the value of collateral arising from the HMI acquisition. At June 30, 2014 we had total borrowing capacity of $31.5 million available for future use, and to cover checks issued in excess of funds on deposit of $2.0 million at June 30, 2014.

Selected Unaudited Consolidated Financial Information (in thousands of dollars)

	Canadian Credit Facility	**US Credit Facility**
Maximum borrowings under credit facility	$15.0 million	$ 84.3 million (US$79.0 million)
Credit facility expiry date	August 7, 2016	April 27, 2017
Available to borrow	$ 15.0 million	$ 61.0 million (US$ 57.2 million)
Credit facility borrowings	$ 6.0 million	$ 38.5 million (US$ 36.1 million)
Unused credit facility available	$ 9.0 million	$ 22.5 million (US$ 21.1 million)
Financial covenants:		
	Covenant does not apply when the unused credit facility available exceeds $2.0 million, which it did at June 30, 2014	Covenant does not apply when the unused credit facility available exceeds US$9.4 million, which it did at June 30, 2014

The terms of the agreements with our lenders provide that dividends cannot be paid to our shareholders in the event that our subsidiaries are not compliant with their financial covenants. Our operating subsidiaries were compliant with all required credit ratios as at June 30, 2014. Accordingly there were no restrictions on dividends arising from non-compliance with financial covenants.

Our debt management strategy is to roll and renew (as opposed to repay and retire) our revolving credit facilities in Canada and the US when they expire in August 2016 and April 2017, respectively. We do not intend to restrict future dividends in order to fully extinguish our bank debt obligations upon their maturity. The amount of bank debt that will actually be drawn on our available revolving credit facilities will depend upon the seasonal and cyclical needs of the business and on our cash generating capacity going forward. When making future dividend decisions, we will consider the amount of financial leverage, and therefore bank debt, we believe is appropriate given existing and expected market conditions and available business opportunities. We do not target a specific financial leverage amount. We believe our current credit facilities are sufficient to finance our working capital needs and market expansion strategy.

5.4 Contractual Obligations

There were no significant changes in our contractual commitments outside of the normal course of business, compared with those set forth in our 2013 Annual Report, available on SEDAR at www.sedar.com.

5.5 Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

5.6 Financial Instruments

Financial assets include cash and cash equivalents and current and long-term receivables, which are measured at amortized cost. Financial liabilities include bank indebtedness, accounts payable and accrued liabilities, income taxes payable and finance lease obligations which are measured at amortized cost. The carrying values of our cash and cash equivalents, accounts receivable, income taxes payable, accounts payable and accrued liabilities approximate their fair values due to the relatively short period to maturity of the instruments. The fair value of long-term receivables and finance lease obligations are not expected to differ materially from carrying value given the interest rates being charged and term to maturity. The carrying values of the credit facilities approximate their fair values due to the existence of floating market-based interest rates.

5.7 Share Data

As at August 13, 2014, the date of this MD&A, we had 16,539,378 common shares issued and outstanding. In addition, at August 13, 2014 we had outstanding 38,001 performance shares and 172,075 restricted shares under the terms of our long-term incentive plan. The performance and restricted shares can be settled in common shares of the Company issued from treasury, shares purchased by us in the market, or in an amount of cash equal to the fair value of our common shares, or any combination of the foregoing. The restricted and performance shares vest over periods of up to three years and we intend to issue common shares from treasury to settle these obligations as they vest.

5.8 Dividends

In the second quarter of 2014, we declared a quarterly dividend of $0.045 per share, which was paid on July 31, 2014 to shareholders of record as at July 18, 2014. On August 13, 2014 we declared a quarterly dividend of $0.045 per share, payable on October 31, 2014 to shareholders of record as at October 20, 2014. The Board regularly assesses our dividend strategy, giving due consideration to anticipated cash needs for additional working capital to support growing the business, appropriate debt levels, acquisition opportunities which may be available, expected market conditions, demand for our products, and other factors.

6.0 Related Party Transactions

There were no material related party transactions in the three or six months ended June 30, 2014 or in the comparative periods in the prior year.

7.0 Critical Accounting Estimates & Adoption of Changes in Accounting Policies

7.1 Critical Accounting Estimates

The preparation of financial statements in accordance with IFRS requires that we make estimates and assumptions that can have a material impact on our results of operations as reported on a periodic basis. We base our estimates and assumptions on past experience and other factors that are deemed reasonable under the circumstances. Actual results could differ from these estimates. The critical estimates used in preparing our financial statements are:

Accounts Receivable Provision: Due to the nature of our business and the credit terms we provide to our customers, we anticipate that a certain portion of required customer payments will not be made, and we maintain an allowance for these doubtful accounts. The allowance is based on our estimate of the potential of recovering our accounts receivable, and incorporates current and expected collection trends.

Deferred Income Taxes: We are required to make estimates and assumptions regarding future business results, as well as the amount and timing of certain future discretionary tax deductions available to us. These estimates and assumptions can have a material impact upon the amount of deferred income tax assets and liabilities that we recognize.

Business combinations: Estimation is required in allocating the purchase price paid for HMI to the identifiable assets acquired. The process of allocating the purchase price takes into account the nature and condition of the assets acquired.

7.2 Adoption of New Accounting Policies

There were no new standards effective January 1, 2014 that have an impact on the Company's Interim Financial Statements. The following new standards and interpretations have not yet been adopted:

IFRS 9, *Financial Instruments ("IFRS 9")*

IFRS 9 will replace IAS 39, *Financial Instruments: Recognition and Measurement* ("IAS 39"). IFRS 9 will replace the multiple classification and measurement models in IAS 39 with a single model that has only two classification categories: amortized cost and fair value. The new standard also requires a single impairment method to be used, provides additional guidance on the classification and measurement of financial liabilities, and provides a new general hedge accounting standard.

The mandatory effective date has been set for January 1, 2018, however early adoption of the new standard is permitted. The Company does not intend to early adopt IFRS 9 in its consolidated financial statements for the annual period beginning on January 1, 2015. The adoption of IFRS 9 is currently not expected to have a material impact on the consolidated financial statements given of the nature of the Company's operations and the types of financial instruments that it currently holds however the Company will continue to assess the extent of impact as the mandatory adoption date approaches.

IFRS 15, *Revenue from Contracts with Customers ("IFRS 15")*

IFRS 15 is effective for fiscal years commencing on or after January 1, 2017 and will replace IAS 18 *Revenue* and a number of revenue related standards and interpretations. IFRS 15 contains a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have also been introduced, which may affect the amount and/or timing of revenue recognized.

The Company intends to adopt IFRS 15 in its financial statements for the annual period beginning on January 1, 2017. The Company is assessing the impact of this new standard but does not expect the amendments to have a material impact on the consolidated financial statements.

8.0 Risks and Uncertainties

We are exposed to a number of risks and uncertainties in the normal course of business that could have a negative effect on our financial condition or results of operations. We identify significant risks that we were aware of in our Annual Information Form dated March 10, 2014, and in our Information Circular dated March 28, 2014. Both documents are available to readers at www.sedar.com.

In March 2014 certain trade sanctions were imposed against Russia, in response to that country's actions in the Crimean peninsula of Ukraine. Approximately 2% of our sales are generated by products sourced from Russia. To date, the limited sanctions imposed have not impacted our purchases from Russia. However we are closely monitoring developments in the Ukraine that could lead to additional trade sanctions that might affect future sourcing of Russian product for resale in North America.

9.0 Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate disclosure controls and procedures ("DC&P") and internal control over financial reporting ("ICFR"). Any systems of DC&P and ICFR, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to information required to be disclosed and financial statement preparation and presentation.

Our management has limited the scope of its design of DC&P and ICFR to exclude controls, policies and procedures of HMI, which we acquired on April 28, 2014. For the quarter ended June 30, 2014, HMI accounted for $6.7 million of our consolidated revenues and $0.5 million of profit. As at June 30, 2014, HMI accounted for $9.8 million of our current assets, $5.0 of our non-current assets, $2.4 of our current liabilities and nil of our non-current liabilities.

There have been no changes in our ICFR during the quarter ended June 30, 2014 that have materially affected, or are reasonably likely to materially affect, our ICFR.

10.0 Note Regarding Forward Looking Information

Certain statements in this MD&A contain forward-looking information within the meaning of applicable securities laws in Canada ("forward-looking information"). The words "anticipates", "believes", "budgets", "could", "estimates", "expects", "forecasts", "intends", "may", "might", "plans", "projects", "schedule", "should", "will", "would" and similar expressions are often intended to identify forward-looking information, although not all forward-looking information contains these identifying words.

The forward-looking information in this MD&A includes, but is not limited to: that we anticipate continued year-over-year sales growth through the second half of 2014 supported by the continued US market recovery, implementation of our business strategies, the positive foreign exchange impact of a weaker Canadian dollar, and the addition of the HMI business, partially offset by a recent softening trend in prices for some hardwoods lumber species; that the National Association of Homebuilders is calling for 1.038 million new housing starts in 2014, somewhat lower than previous estimates, but still up 12.3% over 2013; that renovation spending in the US is expected to rise 6.5% year over year according to the Home Improvement Research Institute, and non-residential construction is expected to increase 11.6% according to McGraw Hill Construction estimates; that in the Canadian market, 2014 housing starts are expected to remain unchanged from 2013 levels, while growth in the renovation and commercial construction markets is expected to be in line with inflation; that our focus in the second half of 2014 will be on continuing to expand our US market share and successfully integrating our newly acquired HMI business. We are also actively pursuing our "Leverage Imports" and "Strengthen Commercial" strategies; that going forward, we have a strong and experienced management team in place to run the business and execute our strategy while CEO Lance Blanco recovers from a cycling accident that occurred in late July; that the Board of Directors will continue to review our financial performance and assess quarterly dividend payments on a regular basis; our perspective that in terms of cash utilization, our primary focus through the balance of 2014 will remain on retaining the cash necessary to finance the significant market opportunity in the US and keeping our balance sheet strong to support strategic acquisitions; that we believe we have made sufficient expenditures to sustain productive capacity of our business as it relates to our needs for property, plant and equipment; that our acquisition of HMI on April 28, 2014 will increase our future capital expenditure needs as the HMI business requires ongoing investment in machinery and equipment; that we anticipate that additional annual capital expenditure requirements of approximately $0.6 million will be required to maintain the productive capacity of HMI; that our debt management strategy is to roll and renew (as opposed to repay and retire) our revolving credit facilities in Canada and the US when they expire in August 2016 and April 2017, respectively; that we do not intend to restrict future dividends in order to fully extinguish our bank debt obligations upon their maturity; that the amount of bank debt that will actually be drawn on our available revolving credit facilities will depend upon the seasonal and cyclical needs of the business and on our cash generating capacity going forward; that when making future dividend decisions, we will consider the amount of financial leverage, and therefore bank debt, we believe is appropriate given existing and expected market conditions and available business opportunities; that we do not target a specific financial leverage amount; and that we believe our current credit facilities are sufficient to finance our working capital needs and market expansion strategy.

The forecasts and projections that make up the forward-looking information are based on assumptions which include, but are not limited to: there are no material exchange rate fluctuations between the Canadian and US dollar that affect our performance; the general state of the economy does not worsen; we do not lose any key personnel; there are no decreases in the supply of, demand for, or market values of hardwood lumber or sheet goods that harm our business; we do not incur material losses related to credit provided to our customers; our products are not subjected to negative trade outcomes; we are able to sustain our level of sales and EBITDA margins; we are able to grow our business long term and to manage our growth; there is no new competition in our markets that leads to reduced revenues and profitability; we do not become subject to more stringent regulations; importation of products manufactured with hardwood lumber or sheet goods does not increase and replace products manufactured in North America; our management information systems upon which we are dependent are not impaired; our insurance is sufficient to cover losses that may occur as a result of our operations; and, the financial condition and results of operations of our business upon which we are dependent is not impaired.

The forward-looking information is subject to risks, uncertainties and other factors that could cause actual results to differ materially from historical results or results anticipated by the forward-looking information. The factors which could cause results to differ from current expectations include, but are not limited to: exchange rate fluctuations between the Canadian and US dollar could affect our performance; our results are dependent upon the general state of the economy; we depend on key personnel, the loss of which could harm our business; decreases in the supply of, demand for, or market values of hardwood lumber or sheet goods could harm our business; we may incur losses related to credit provided to our customers; our products may be subject to negative trade outcomes; we may not be able to sustain our level of sales or EBITDA margins; we may be unable to grow our business long term to manage any growth; competition in our markets may lead to reduced revenues and profitability; we may become subject to more stringent regulations; importation of products manufactured with hardwood lumber or sheet goods may increase, and replace products manufactured in North America; we are dependent upon our management information systems; our insurance may be insufficient to cover losses that may occur as a result of our operations; we are dependent upon the financial condition and results of operations of our business; our credit facilities affect our liquidity, contain restrictions on our ability to borrow funds, and impose restrictions on distributions that can be made by our operating limited partnerships; our future growth may be restricted by the payout of substantially all of our operating cash flow; and, other risks described in our Annual Information Form our Information Circular and in this MD&A.

All forward-looking information in this MD&A is qualified in its entirety by this cautionary statement and, except as may be required by law, we undertake no obligation to revise or update any forward-looking information as a result of new information, future events or otherwise after the date hereof.