Management's Discussion and Analysis

November 7, 2014

This management's discussion and analysis ("MD&A") has been prepared by Hardwoods Distribution Inc. ("HDI" or the "Company") as of November 7, 2014. This MD&A covers our unaudited interim condensed consolidated financial statements as at and for the three and nine month periods ended September 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 Standard No. 34, *Interim Financial Reporting* ("IAS 34") 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 condensed 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 a 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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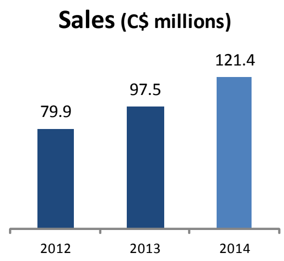
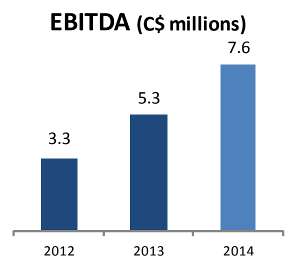
1.0 Executive Summary

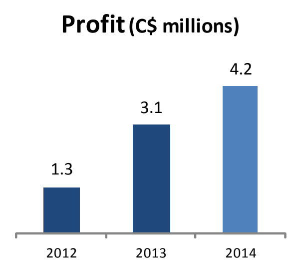
1.1 Overview

We continued to achieve strong, profitable growth in the third quarter and first nine months of 2014, generating record sales results, near-record EBITDA, and growing profits.

Three Months Ended September 30th:

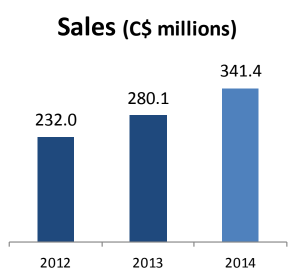


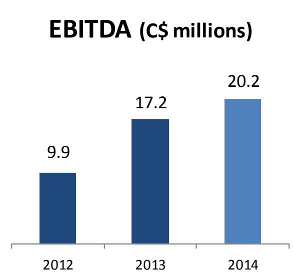


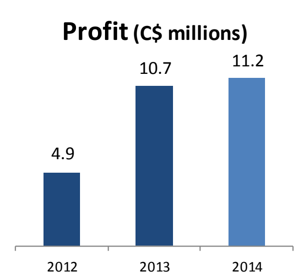


For the three months ended September 30, 2014, total sales climbed 24.5% to $121.4 million, while EBITDA increased 43.4% to $7.6 million, compared to the same period in 2013. Profit for the period increased to $4.2 million.

Nine Months Ended September 30th:







For the nine months ended September 30, 2014, sales increased 21.9% to $341.4 million, EBITDA climbed 17.4% to $20.2 million and we increased profit for the period to $11.2 million.

Organic growth was a key contributor to our strong sales performance in both the third quarter and year-to-date periods as we continued to implement business strategies focused on market expansion. The addition of Hardwoods of Michigan ("HMI"), the integrated, high-quality hardwood lumber producer and exporter we acquired on April 28, 2014, also contributed to our results. Sales results further benefitted from the 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.

Market conditions were generally favourable with the seasonally adjusted annual rate of US housing starts averaging 1,024,000 during the third quarter, up 16.1% from 882,000 in the same period last year according to the US Census Bureau. Product pricing remained mixed with hardwood lumber prices rising and domestic panel prices remaining generally stable compared to the same period last year. Prices for some of our imported products returned to more normal levels on a year-to-date basis, reflecting the absence of preliminary duties of 22% that were added to the price of Chinese plywood imports through much of 2013 due to a trade dispute in the US. These duties did not apply in the current period as the trade case was dismissed in the fourth quarter of 2013.

We reported a gross profit margin of 17.2% for the third quarter and 17.5% for the nine-month period ended September 30, 2014. While these levels were lower than a year ago, we view them as sustainable based on current product pricing, intensity of competition, growing our commercial business, and the addition of the HMI manufacturing business, which carries a somewhat lower gross margin than our traditional distribution business. Expenses remained well in check across the organization with sales and administrative costs continuing to decline as a percentage of revenue. We were successful in increasing cash provided by operating activities by $15.2M for the nine months ended September 30, 2014 as compared to the same period in the prior year. The increase in operating cash flow came primarily through more efficient management of working capital, and allowed us to finance a portion of the HMI acquisition with internally generated cash flow while maintaining a strong balance sheet to support our future growth initiatives.

Based on our continuing strong performance and favourable outlook, our Board of Directors approved a quarterly dividend of $0.045 per share, payable on January 30, 2015 to shareholders of record as at January 20, 2015.

1.2 Outlook

We anticipate continued year-over-year sales growth through the balance of 2014 supported by implementation of our business strategies, the positive foreign exchange impact of a weaker Canadian dollar, and contribution from the acquired HMI business. Market conditions are expected to remain favourable through the end of 2014 and into 2015, but we expect to experience the usual seasonal fourth quarter slowdown as customer activity tapers off during the Thanksgiving and Christmas holiday periods.

Our focus in the fourth quarter and into 2015 will be on continuing to expand our US market share and completing the integration of the 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; and
- 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, our experienced management team will continue to execute on Hardwoods’ established business plans and growth strategy while CEO Lance Blanco recovers from the cycling accident that occurred in late July. Mr. Blanco’s recovery period is expected to extend into the new year. Rob Brown, Hardwoods’ current Chief Financial Officer, will continue as acting Chief Executive Officer during this period, and other senior executives have assumed expanded roles.

The Board of Directors will continue to review our financial performance and assess dividend levels on a regular basis. However, in terms of cash utilization, our primary focus remains on retaining the cash necessary to finance the significant market opportunity in the US and to keep 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 September 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 51% 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 38% 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, approximately 11%, is comprised 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 end 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

3.1 Three Month Periods Ended September 30, 2014 and September 30, 2013

Selected Unaudited Consolidated Financial Information (in thousands of Canadian dollars)

	For the three months Ended September 30 2014	For the three months Ended September 30 2013	$ Increase (Decrease)	% Increase (Decrease)
Total sales	$ 121,398	$ 97,546	$ 23,852	24.5%
Sales in the US (US$)	*86,155*	*70,081*	*16,074*	22.9%
Sales in Canada	*27,525*	*24,812*	*2,713*	10.9%
Gross profit	20,889	17,647	3,242	18.4%
Gross profit %	*17.2%*	*18.1%*		
Operating expenses	(13,877)	(12,753)	1,124	8.8%
Profit from operating activities	7,012	4,894	2,118	43.3%
Add: Depreciation and amortization	582	375	207	55.2%
Earnings before interest, taxes, depreciation and amortization ("EBITDA")	$ 7,594	$ 5,269	$ 2,325	44.1%
Add (deduct):				
Depreciation and amortization	(582)	(375)	(207)	
Net finance income (cost)	7	(372)	379	
Income tax expense	(2,773)	(1,413)	(1,360)	
Profit for the period	$ 4,246	$ 3,109	$ 1,137	36.6%
Basic profit per share	$ 0.26	$ 0.19		
Fully diluted profit per share	0.25	0.19		
Average Canadian dollar exchange rate for one US dollar	1.089	1.038		

Sales

For the three months ended September 30, 2014, total sales increased 24.5% to $121.4 million, from $97.5 million during the same period in 2013. Of the $23.9 million year-over-year increase, $19.5 million was due to stronger underlying sales and $4.4 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$16.1 million, or 22.9%, to US$86.2 million, from US$70.1 million in the same period in 2013. Organic growth accounted for US$7.4 million, or 10.5%, of the increase as a result of stronger underlying sales activity and higher pricing on some product lines. HMI, acquired on April 28, 2014, contributed US$8.7 million, or 12.4%, to the increase in US sales.

Sales in Canada, which comprise approximately one quarter of our revenues, increased by $2.7 million, or 10.9%, year-over-year. 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 September 30, 2014 increased 18.4% to $20.9 million, from $17.6 million in the third quarter of 2013. This $3.3 million improvement reflects the higher sales for the period, partially offset by a lower gross profit margin. As a percentage of sales, third quarter gross profit margin was 17.2%, compared to 18.1% last year. The year-over-year reduction reflects 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. Our entry into targeted commercial market segments also impacted margins as we offered competitive introductory pricing to some of our new accounts.

Operating Expenses

Operating expenses increased to $13.9 million in the third quarter of 2014, from $12.8 million during the same period last year. The $1.1 million increase primarily reflects $0.6 million in incremental costs from the acquired HMI business 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 11.4% of sales in the three months ended September 30, 2014, compared to 13.1% during the same period in 2013.

EBITDA

We generated EBITDA of $7.6 million in the third quarter of 2014, an increase of $2.3 million or 44.1%, from $5.3 million in the same period last year. The increase primarily reflects the $3.2

million increase in gross profit, offset by the $0.9 million increase in operating expense net of depreciation and amortization.

Net Finance Income (Cost)

(in thousands of Canadian dollars)	Three months ended September 30 2014	Three months ended September 30 2013	$ Increase (Decrease)
Finance expense:			
Interest on bank indebtedness	$ (337)	$ (312)	$ 25
Accretion of finance lease obligation	(29)	(26)	3
Foreign exchange losses	-	(166)	(166)
Total finance expense	(366)	(504)	(138)
Finance income:			
Interest on trade receivables, customer notes, and employee loans	105	132	(27)
Foreign exchange gain	268	-	268
Total finance income	373	132	241
Net finance income (cost)	$ 7	$ (372)	$ (379)

Third quarter net finance income was $7,000, compared to a net finance cost of $0.4 million during the same period in 2013. The year-over-year improvement 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 September 30, 2014, a weakening of the Canadian dollar resulted in a foreign exchange gain of $0.3 million on intercompany debt, compared to a strengthening of the Canadian dollar and a corresponding $0.2 million foreign exchange loss in the comparative period in 2013.

Income Tax Expense

Income tax expense increased to $2.8 million in the third quarter of 2014, from $1.4 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 September 30, 2014 was $4.2 million, compared to $3.1 million during the same period in 2013. The $1.1 million increase in profit reflects the $2.3 million increase in EBITDA and the $0.4 million increase in net finance income, partially offset by a $0.2 million increase in depreciation and amortization, and a $1.4 million increase in income tax expense.

3.2 Nine Month Period Ended September 30, 2014 and September 30, 2013

Selected Unaudited Consolidated Financial Information (in thousands of Canadian dollars)	For the Nine months Ended September 30 2014	For the Nine months Ended September 30 2013	$ Increase (Decrease)	% Increase (Decrease)
Total sales	$ 341,370	$ 280,146	$ 61,224	21.9%
Sales in the US (US$)	*239,217*	*203,528*	*35,689*	17.5%
Sales in Canada	*79,618*	*71,856*	*7,762*	10.8%
Gross profit	59,680	51,628	8,052	15.6%
Gross profit %	*17.5%*	*18.4%*		
Operating expenses	(40,975)	(35,522)	5,453	15.4%
Profit from operating activities	18,705	16,106	2,599	16.1%
Add: Depreciation and amortization	1,535	1,046	489	46.7%
Earnings before interest, taxes, depreciation and amortization ("EBITDA")	$ 20,240	$ 17,152	$ 3,088	18.0%
Add (deduct):				
Depreciation and amortization	(1,535)	(1,046)	(489)	
Net finance cost	(342)	(103)	(239)	
Income tax expense	(7,156)	(5,311)	(1,845)	
Profit for the period	$ 11,207	$ 10,692	$ 515	4.8%
Basic profit per share	$ 0.68	$ 0.65		
Fully diluted profit per share	0.67	0.64		
Average Canadian dollar exchange rate for one US dollar	1.094	1.023		

Sales

For the nine months ended September 30, 2014 total sales increased to $341.4 million, from $280.1 million in the first nine months of 2013, an increase of $61.2 million, or 21.9%. Higher underlying sales accounted for $44.2 million of the sales growth, while $17.0 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$35.7 million, or 17.5%, in the first nine months of 2014 compared to the same period in the prior year. US$20.7 million of this sales increase came from existing operations, representing an organic growth rate of 10.2%. Incremental revenue from acquired businesses provided sales of US$15.0 million or 7.4% sales growth. In Canada, sales in the first nine months of 2014 increased by $7.8 million, or 10.8%, year over year, entirely on organic growth.

Gross Profit

Gross profit for the first nine months of 2014 increased to $59.7 million, from $51.6 million in the first nine months of 2013. The 15.6% improvement reflects increased sales, partially offset by a lower gross profit margin. As a percentage of sales, gross profit decreased to 17.5% in the first nine months of 2014, from 18.4% during the same period in 2013. Gross profit margin in the first nine months of 2013 was unusually strong, aided by a rapid increase in Chinese import panel prices as the result of a trade action, in the US, against the product at that time. The trade action was later dismissed. The year-over-year decline in gross profit margin also reflects the impact of competitive conditions, the acquisition of HMI, and lower margins on newly won commercial account business.

Operating Expenses

Operating expenses increased $5.5 million to $41.0 million in the first nine months of 2014, from $35.5 million during the same period in 2013. The increase reflects $2.6 million in higher costs incurred to support growth, $1.8 million of higher expense due to the impact of a weaker Canadian dollar on translation of US operating expenses, and $1.1 million in incremental costs from the acquired HMI business. As a percentage of sales, operating expenses improved to 12.0% of sales during the nine-month period ended September 30, 2014, compared to 12.7% in the same period in 2013.

Depreciation and Amortization

Depreciation and amortization for the first nine months of 2014 was $1.5 million, compared to $1.0 million in the same period in 2013. The $0.5 million increase reflects depreciation on additional property, plant and equipment acquired by the business, including assets acquired as part of the HMI manufacturing business acquisition.

EBITDA

For the nine months ended September 30, 2014, EBITDA increased to $20.2 million, from $17.2 million during the same period in 2013. The $3.0 million improvement reflects the $8.0 million increase in gross profit, partially offset by a $5.0 million increase in operating expenses, net of depreciation and amortization.

Net Finance Income (Cost)

(in thousands of Canadian dollars)		Nine months ended September 30 2014		Nine months ended September 30 2013		$ Increase (Decrease)
Finance expense:						
Interest on bank indebtedness	$	(875)	$	(790)	$	85
Accretion of finance lease obligation		(82)		(70)		12
Foreign exchange losses		-		-		-
Total finance expense		(957)		(860)		97
Finance income:						
Interest on trade receivables						
customer notes, and employee loans		325		373		(48)
Foreign exchange gain		290		384		(94)
Total finance income		615		757		(142)
Net finance income (cost)	$	(342)	$	(103)	$	239

Net finance cost during the nine-months ended September 30, 2014 was $0.3 million, compared to a net finance cost of $0.1 million during the same period in 2013. As shown in the preceding table, the main factor in this increase was a $0.1 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 nine months ended September 30, 2013, a weakening of the Canadian dollar resulted in a foreign exchange gain of $0.4 million on this intercompany debt, compared to $0.3 million in the same period in the current year.

Income Tax Expense

Income tax expense increased to $7.2 million in the first nine months of 2014, from $5.3 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 nine months ended September 30, 2014, we generated profit of $11.2 million, compared to $10.7 million during the same period in 2013. The $0.5 million increase reflects the $3.1 million improvement in EBITDA, partially offset by a $0.5 million increase in depreciation and amortization, a $0.2 million increase in net finance cost, and a $1.9 million increase in income tax expense.

4.0 Quarterly Financial Information and Seasonality

(in thousands of dollars)	Q3 2014	Q2 2014	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012
Total sales	$ 121,398	$ 119,038	$ 100,934	$ 91,069	$ 97,546	$ 95,617	$ 86,983	$ 74,133
Profit	4,246	3,996	2,965	2,375	3,109	4,403	3,180	1,313
Basic profit per share or unit	0.26	0.24	0.18	0.14	0.19	0.27	0.19	0.08
Fully diluted profit per share or unit	0.25	0.24	0.18	0.14	0.19	0.27	0.19	0.08
EBITDA	7,594	7,543	5,103	4,216	5,269	6,740	5,143	2,407

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 acquisition of HMI in the second quarter of 2014.

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 September 30			Nine months ended September 30		
	2014	2013	$ Change	2014	2013	$ Change
Cash provided by operating activities before changes in non-cash working capital	$ 6,354	$ 3,332	$ 3,022	$ 16,063	$ 13,070	$ 2,993
Changes in non-cash working capital	(1,413)	17	(1,430)	(12,692)	(24,925)	12,233
Net cash provided by (used in) operating activities	4,941	3,349	1,592	3,371	(11,855)	15,226
Net cash provided by (used in) investing activities	(1,226)	(233)	(993)	(16,911)	(3,317)	(13,594)
Net cash provided by (used in) financing activities	(3,720)	(3,111)	(609)	13,478	15,094	(1,616)
Increase (decrease) in cash	(5)	5	(10)	(62)	(78)	16
Cash, beginning of period	21	11	10	78	94	(16)
Cash, end of period	$ 16	$ 16	$ -	$ 16	$ 16	$ -

In the three months ended September 30, 2014, cash provided by operating activities increased to $4.9 million. This compares to cash provided by operating activities of $3.3 million during the same period in 2013. Cash provided by operating activities, before changes in non-cash working capital, increased by $3.0 million. This primarily reflects the $2.3 million increase in third quarter EBITDA. Investment in non-cash working capital was $1.4 million higher in the third quarter of 2014 compared to the same period in the prior. An analysis of changes in working capital is provided in section 5.2 of this report.

For the nine months ended September 30, 2014, cash provided by operating activities was $3.4 million, compared to cash used of $11.9 million during the same period in 2013. Cash provided by operating activities, before changes in non-cash working capital, increased by $3.0 million. This primarily reflects the $3.1 million increase in year to date EBITDA. Investment in non-cash working capital for the nine months ended September 30, 2014 decreased by $12.2 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 used in investing activities

Net cash used in investing activities increased by $1.0 million and $13.6 million, respectively, in the third quarter and first nine months of 2014, compared to the same periods in 2013. The third quarter of 2014 increase primarily reflects a $1.2 million holdback related to the acquisition of HMI that was paid during the quarter, offset by an increase of $0.2 million in long-term receivables collected. The year-to-date increase primarily relates to the $15.3 million acquisition of HMI and the $1.2 million holdback paid on the acquisition of HMI as previously discussed, offset by $3.0 million invested in the import lumber business acquired in Leland, North Carolina during the same period in 2013. Net cash 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.

To date, we believe we have made sufficient expenditures to sustain the 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 as the 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 September 30, 2014, principal payments on automobile finance lease obligation were $0.2 million (2013 - $0.2 million) and for the nine months ended September 30, 2014 were $0.7 million (2013 - $0.6 million).

Net cash provided by financing activities

Although our utilization of cash to make acquisitions increased by $1.0 million in the third quarter and $13.7 million in the first nine 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 used in financing activities increased by just $0.6 million in the third quarter and net cash provided by financing activities decreased by $1.6 million in the first nine months of 2014 compared to a year ago, despite completing the HMI acquisition and continuing to invest in 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 $126.2 million as at September 30, 2014, compared to $98.4 million at December 31, 2013 and $110.1 million at September 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 nine months ended September 30, 2014 and 2013 is provided below.

(in thousands of Canadian dollars) Source (use) of funds	Three months ended September 30, 2014	Three months ended September 30, 2013	Nine months ended September 30, 2014	Nine months ended September 30, 2013
Accounts receivable	$ 619	$ 2,325	$ (4,527)	$ (11,072)
Inventory	(1,271)	(2,214)	(10,003)	(14,658)
Prepaid expenses	(170)	(675)	(584)	(456)
Accounts payable, accrued liabilities and provisions	(591)	581	2,422	1,261
Increase in non-cash operating working capital	$ (1,413)	$ 17	$ (12,692)	$ (24,925)

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 September 30, 2014	As at December 31, 2013
Cash	$ (16)	$ (78)
Bank indebtedness	42,199	27,881
Net Debt	42,183	27,803
Shareholders' equity	103,540	90,683
Total Capitalization	$ 145,723	$ 118,486
Net debt to total capitalization	28.9%	23.5%
Previous 12 months EBITDA	$ 24,456	$ 21,368
Net debt to previous 12 months EBITDA	1.7	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 $14.4 million to $42.2 million at September 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.

Overall, net debt compared to total capitalization stood at 28.9% as at September 30, 2014, compared to 23.5% at December 31, 2013. At September 30, 2014 our ratio of net debt-to-EBITDA for the previous 12 months was 1.7 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 five 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 September 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 on April 27, 2017, with monthly payments based on a five-year amortization. Monthly payments on the term loan reduce the total credit facility and so the credit facility at September 30, 2014 is comprised of US$75.0 million available under revolving credit facilities and US$3.8 million under the term loan.

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 September 30, 2014 we had total borrowing capacity of $34.0 million available for future use, and to cover checks issued in excess of funds on deposit of $0.6 million at September 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	$ 88.3 million (US$78.8 million)
Credit facility expiry date	August 7, 2016	April 27, 2017
Available to borrow	$ 15.0 million	$ 64.0 million (US$ 57.2 million)
Credit facility borrowings	$ 8.9 million	$ 36.1 million (US$ 32.3 million)
Unused credit facility available	$ 6.1 million	$ 27.9 million (US$ 24.9 million)
Financial covenants:		
	Covenant does not apply when the unused credit facility available exceeds $2.0 million, which it did at September 30, 2014	Covenant does not apply when the unused credit facility available exceeds US$9.4 million, which it did at September 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 September 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, we believe bank debt 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, and 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 November 7, 2014, the date of this MD&A, we had 16,539,378 common shares issued and outstanding. In addition, at November 7, 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 third quarter of 2014, we declared a quarterly dividend of $0.045 per share, which was paid on October 31, 2014 to shareholders of record as at October 20, 2014. On November 7, 2014 we declared a quarterly dividend of $0.045 per share, payable on January 30, 2015 to shareholders of record as at January 20, 2015. 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 nine month periods ended September 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 our 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. We do not intend to early adopt IFRS 9 in our 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 our operations and the types of financial instruments that we currently hold; however, we 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.

We intend to adopt IFRS 15 in our financial statements for the annual period beginning on January 1, 2017. We are assessing the impact of this new standard but do not expect the amendments to have a material impact on our 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.

Since March 2014, certain trade sanctions have been imposed against Russia in response to that country's actions in the Ukraine. Approximately 2% of our sales are generated by products sourced from Russia. To date, sanctions imposed have not impacted these products; however, we are closely monitoring developments 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 September 30, 2014, HMI accounted for $9.5 million of our consolidated revenues and $0.6 million of profit. As at September 30, 2014, HMI accounted for $8.3 million of our current assets, $4.6 million of our non-current assets, $0.7 million of our current liabilities and nil of our non-current liabilities.

There have been no changes in our ICFR during the quarter ended September 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: We anticipate continued year-over-year sales growth through the balance of 2014; market conditions are expected to remain favourable through the end of 2014 and into 2015, but we expect to experience the usual seasonal fourth quarter slowdown as customer activity tapers off during the Thanksgiving and Christmas holiday periods; the seasonally adjusted annual rate of US housing starts average is 1,024,000 during the third quarter, up from 882,000 in the same period last year according to the US Census Bureau, our focus in the fourth quarter and into 2015 will be on continuing to expand our US market share and completing the integration of the HMI business; we are actively pursuing our "Leverage Imports" and "Strengthen Commercial" strategies; Mr. Blanco's recovery period is expected to extend into the new year; the Board of Directors will continue to review our financial performance and assess distribution levels on a regular basis in terms of cash utilization; our primary focus remains on retaining the cash necessary to finance the significant market opportunity in the US and to keep our balance sheet strong to support strategic acquisitions; we estimate about 60% of our products are used in new residential construction and the balance of our products end up in other sectors of the economy not associated with residential construction; we anticipate that additional annual capital expenditure requirements of approximately $0.6 million will be required to maintain the productive capacity of this business; our investment in working capital fluctuates from quarter-to-quarter based on many factors including those discussed in this MD&A; the first and fourth quarters are seasonally slower periods for construction activity, which may result in reduced demand for hardwood products, lower sales and lower working capital requirements in these quarters; 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 believe our current credit facilities are sufficient to finance our working capital needs and market expansion strategy; 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; the amount of bank debt that will actually be drawn on our available credit facilities will depend upon the seasonal and cyclical needs of the business and on our cash generating capacity going forward; we do not intend to restrict future dividends in order to fully extinguish our bank debt obligations upon their maturity; 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 allowance for doubtful accounts is based on our estimate of the potential of recovering our accounts receivable, and incorporates current and expected collection trends; 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; we do not expect the adoption of IFRS 9 and IFRS 15 to have a material impact on our consolidated financial statements; developments in the Ukraine could lead to additional trade sanctions that might affect future sourcing of Russian product for resale in North America; 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; our method of calculating non GAAP measures as noted in this MD&A may differ from the method used by other issuers to calculate these measures; and credit 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 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.