



WIRE & WIRE PRODUCTS

ESTABLISHED IN 1964



**2018
Annual Report**

Since 1964, Tree Island Steel has been making products from steel wire for a diverse range of customers for industrial, construction, agricultural, and specialty applications.

Our products include concrete reinforcing mesh, fencing, galvanized wire, bright wire, a broad array of fasteners, stucco reinforcing products, and other fabricated wire products. We market these products under the Tree Island®, Halsteel®, True Spec®, K-Lath®, TI Wire® and Tough Strand® brand names.

Listed on the Toronto Stock Exchange (“TSX”), our shares trade under the symbol TSL.

MANAGEMENT DISCUSSION AND ANALYSIS..... 2
CONSOLIDATED FINANCIAL STATEMENTS..... 19
SHAREHOLDER INFORMATION..... back cover



Mesh rolls for earth reinforcement of highways and roadways.

TO OUR SHAREHOLDERS

Letter to Shareholders

2018 marked another year of rapid change with an evolving business environment for Tree Island. We experienced a period of escalating raw material input costs, the imposition of U.S. Section 232 tariffs on imported steel, the onset of Canadian counter-tariffs and competitive pricing pressures from low-cost imports. Section 232 and with other trade actions brought about additional challenges with disruptions on demand and supply chains for the Company and our customers. This environment is likely to continue until the trade actions are eliminated.

For Tree Island, 2018 was also a year of improved margins and profitability. We remained steadfast to our commitments to improve operational efficiencies, rationalize low margin products, and maintain pricing discipline. We continue to leverage our competitive advantages, which include the quality of our products and exceptional service to further strengthen our business. In addition to our focus on operational excellence across our manufacturing activities, we also made strategic investments in our facilities and upgrades to our aging production equipment. These investments improved efficiencies, support our long-term objectives and strengthen our cost-sensitive leadership position.

Looking forward to 2019, the outlook from industry indicators and forecasts remains positive for our commercial end markets. Forecasts for the residential and industrial markets indicate modest growth over the prior year. While the overall outlook for 2019 remains positive, we are concerned about the market dynamics with Section 232 in place and its impact on domestic prices of our primary raw material, which are well above international levels. As import tariffs were not applied to certain downstream steel products, placing us at a competitive disadvantage to manufacturers who continue to have access to steel from foreign markets that are not subject to Section 232.

As the supplier of choice to our customers, we maintain a sustainable business with long-term profitability. We will continue to build on the progress that was made in the last year. Our focus remains on our priorities in optimizing our cost structure and improving the productivity of all of our manufacturing, selling and administrative activities, investing in our people and facilities, and capitalizing on the competitive advantages that are available to us.

As in prior years, we would like to thank all our employees, customers and shareholders for their continued support. We would not have been able to address the challenges we experienced in 2018 without the trust and confidence placed on the Tree Island brand. We look forward to building on the progress that was made over the past year and to the opportunities that lie ahead.

Sincerely,

Amar S. Doman
Chairman of the Board of Directors

Dale R. MacLean
Director, President and Chief Executive Officer

MANAGEMENT DISCUSSION AND ANALYSIS

December 31, 2018 and 2017

The following is a discussion of the financial condition and results of operations of Tree Island Steel ("Tree Island" or the "Company") and its wholly owned operating subsidiary Tree Island Industries (together with Tree Island Steel, referred to as "Tree Island"). This discussion is current to February 20, 2019 and should be read in conjunction with the consolidated financial statements for the year ended December 31, 2018. Tree Island Steel's consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") applicable to the preparation of financial statements and are reported in Canadian dollars. Additional information relating to Tree Island Steel, including the audited consolidated financial statements and Annual Information Form ("AIF") for the year ended December 31, 2018, can be found at www.sedar.com or on Tree Island Steel's website at www.treeisland.com.

1 FORWARD LOOKING STATEMENTS AND RISK

This management's discussion and analysis ("MD&A") includes forward-looking information with respect to Tree Island Steel, including our business, operations and strategies, as well as financial performance and conditions. The use of forward-looking words such as, "may," "will," "expect" or similar variations generally identify such statements. Any statements that are not statements of historical fact should be considered to be forward-looking statements. Although we believe that the forward-looking statements are reasonable, they involve risks and uncertainties, including the risks and uncertainties discussed under the heading "Risks Relating to the Company's Business" in the Company's AIF for the year ended December 31, 2018.

The forward-looking statements contained herein reflect management's current beliefs and are based upon certain assumptions that management believes to be reasonable based on the information currently available to management. By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and a number of factors could cause actual events or results to differ materially from the results discussed in the forward-looking statements. In evaluating these statements, prospective investors should specifically consider various factors including the risks outlined herein under the heading "Risk Factors" which may cause actual results to differ materially from any forward-looking statement. Such risks and uncertainties include, but are not limited to: general economic, market and business conditions, the cyclical nature of our business and demand for our products, financial condition of our customers, competition, volume and price pressure from import competition, deterioration in the Company's liquidity, disruption in the supply of raw materials, volatility in the costs of raw materials, transportation costs, foreign exchange fluctuations, leverage and restrictive covenants, labour relations, trade actions, dependence on key personnel and skilled workers, intellectual property risks, energy costs, un-insured loss, credit risk, operating risk, management of growth, changes in tax, environmental and other legislation, and other risks and uncertainties set forth in our publicly filed materials.

This MD&A has been reviewed by the Board of Directors of Tree Island Steel and its Audit Committee, and contains information that is current as of the date of this MD&A, unless otherwise noted. Events occurring after that date could render the information contained herein inaccurate or misleading in a material respect. Readers are cautioned not to place undue reliance on this forward-looking information and management of Tree Island undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise except as required by applicable securities law.

2 NON-IFRS MEASURES

References in this MD&A to “EBITDA” are to provide an EBITDA that we define as operating income and adding back depreciation and foreign exchange gains or losses. EBITDA is not a measure recognized by IFRS and does not have a standardized meaning prescribed by IFRS. We believe that providing an EBITDA is an important supplemental measure for evaluating our performance. You are cautioned that our EBITDA should not be construed as an alternative to net income or loss determined in accordance with IFRS, nor should it be used as an indicator of performance, cash flows from operating, investing and financing activities, as a measure of liquidity or cash flows. Our method of calculating EBITDA may differ from methods used by other issuers and, accordingly, our EBITDA may not be comparable to similar measures presented by other issuers.

3 TREE ISLAND STEEL

Since 1964, Tree Island has been making products from steel wire for a diverse range of customers and applications. Tree Island Steel, following a conversion from an income trust to a corporate entity, was incorporated under the laws of Canada on August 2, 2012, and the units of the income fund were converted to common shares in Tree Island Steel.

There were 29,183,650 Shares outstanding as of December 31, 2018 and 29,170,955 shares outstanding as of February 20, 2019.

3.1 ORGANIZATIONAL STRUCTURE

Our corporate structure has the following primary entities: Tree Island Industries (“TI Canada”) which is our Canadian operating company as well as the ultimate parent company to our operations in the United States which are managed through our U.S. operating subsidiary, Tree Island Wire. (“TI USA”).

3.2 PRODUCTS

Tree Island is a manufacturer and supplier of premium quality wire products for a broad range of applications. Our goal is to match the appropriate wire product with our customers’ needs. We achieve this by manufacturing most of our products at our own manufacturing facilities, while outsourcing others from qualified manufacturers. We market these products to customers in Canada, the United States and internationally.

We market our products under the following brands:



Our manufactured products offer: consistent, high quality that meet or exceed customers’ needs, ASTM standards and applicable codes; broad range of applications; short lead times; technical support and excellent customer service.

The products we source from other suppliers are generally limited to commodity items, or items we do not produce. Products within this group meet general industry specifications, but are not customized to individual customer requirements. Outsourced products allow us to enhance our relationship with those customers that require competitively priced commodity products. These products typically create complementary pull through for our manufactured products. As a service to our customers, we also use our network of suppliers world-wide to source commodity wire products and direct ship to our customers.

3.3 MARKETS

The following summarizes the markets, key product groups, the specific end-use markets, and regions we serve with of our products:

Markets	Brand	Key Product Groups	Specific End-Use Markets	Regions
Industrial	Tree Island®, TI Wire®	Bright/galvanized/annealed low and high carbon wire	Wire fabricating, industrial applications, OEM manufacturing	North America and International
Agricultural	Tree Island®, Tough Strand®	Game fence and farm fence Vineyard wire and barbed wire	Agriculture, farming	North America
Commercial Construction	Tree Island®, TI Wire®	Welded wire reinforcement mesh Concrete reinforcing products	Commercial construction, mining, infrastructure projects	North America and International
Residential Construction	Tree Island®, Halsteel®, K-Lath®, True Spec®	Collated, bulk and packaged nails Stucco reinforcing mesh	Construction and renovation for new and existing homes	North America and International

3.4 SEASONALITY

Our operations are impacted by the seasonal nature of the various industries we serve, primarily the construction and agriculture industries. Accordingly, revenues, sales volumes and operating results for interim quarters are not necessarily indicative of the results that may be expected for the full fiscal year and fourth quarter results are traditionally lower than other quarters due to the onset of winter and the corresponding reduction in construction and agricultural activities.

4 FULL YEAR 2018 BUSINESS OVERVIEW AND DEVELOPMENT

4.1 BUSINESS OVERVIEW

The business environment in 2018 was challenging in many ways, lead by the escalating prices for our primary raw material and ongoing competitive pricing pressures from low-cost products by foreign manufacturers. The imposition of U.S. Section 232 tariffs on steel imported into the U.S. during the second half of the year, reduced

volumes from the Industrial segment as these products were now subject to a 25% import tariff. Section 232 also brought about the proliferation of lower priced imported products that were not subject to the 25% tariff, which contributed to the compression of margins and reduction in overall shipments.

For the fourth quarter of 2018, revenues were \$44.9 million, a decrease of 17.7% from the same period last year on account of the combined impact of Section 232 and the seasonality of the construction market. We remained steadfast to our commitments to improve operational efficiencies, rationalize low margin products, maintain pricing discipline, and continue to leverage our competitive advantages. As a result, gross profit for the quarter amounted to \$3.7 million and gross margin was 8.2%, compared to \$2.5 million and 4.5% in 2017.

For the year-ended December 31, 2018, total revenues of \$235.3 million were marginally better than the same period last year on lower volumes, resulting from improved average selling prices in relation to the cost of raw materials. Gross profit earned for 2018 amounted to \$25.8 million and the gross profit margin was 11.0%, compared to the gross profit earned in the corresponding period last year of \$18.2 million with a gross profit margin of 7.8%. The improvements in product mix, increased pricing and rationalizing of lower margin products improved profitability and as a result, EBITDA for 2018 amounted to \$13.4 million compared to \$7.0 million in 2017.

In 2018, we invested in new capital equipment during the year, which is being commissioned for operation in 2019. This will support our long-term objectives and strengthen our market and cost leadership positions in mesh and concrete reinforcing products.

4.2 Trade Action Review

4.2.1 U.S. Section 232 Trade Expansion Act

On April 20, 2017, the U.S. administration issued an executive order directing the Commerce Department to investigate whether imports of foreign steel are harming U.S. national security. The directive falls under Section 232 of the Trade Expansion Act of 1962, which allows the U.S. president to restrict trade of goods if such trade is determined to be harmful to U.S. national security.

On March 8, 2018, the President issued Proclamations 9704 and 9705 on Adjusting Imports of Steel and Aluminum into the United States, under Section 232 of the Trade Expansion Act of 1962, as amended (19 U.S.C. 1862), providing for additional import duties for steel mill and aluminum articles, effective March 23, 2018.

From March 23, 2018, certain steel products imported into the U.S. are now subject to additional import duties of 25%. As of June 1, 2018, the United States determined that Canada, Mexico and the member countries of the European Union would no longer receive an exemption for Section 232, and would also be subject to a 25% tariff on certain steel products.

Due to limited availability of domestic sourcing options in the U.S for certain items, Tree Island has imported certain steel products into the United States that are subject to the import duty of 25%. The exposure and financial impact to Tree Island has been mitigated by price increases on the impacted end products to counter the costs associated with the import tariffs.

Certain steel products produced in Canada and sold to U.S. customers are also impacted by the Section 232 tariffs, principally bright and galvanized wire in our Industrial market segment. The Company is passing to our U.S customers the costs increases associated with Section 232 tariffs, but this has also resulted in lower demand to our U.S markets. Tree Island has taken operational actions to adjust production levels to align with the lower demand. These actions helped to mitigate the decrease in sales volume.

4.2.2 Canadian Counter-Tariffs on Steel and Aluminum Products

In response to the trade actions by the U.S. government, Canada imposed similar tariffs and surtaxes against imports of steel, aluminum, and other products. These import tariffs will only apply to goods originated from the United States and took effect on July 1, 2018. The Canadian retaliatory tariffs are not having an impact on our costs or profitability. The Company does not have any significant sales into Canada from its U.S. subsidiaries that would be impacted by the Canadian import tariffs.

4.2.3 Canadian Safeguard on Steel

The Canadian government issued provisional safeguard measures imposing quotas for 200 days on the import of seven classes of steel goods, which includes wire rod, the Company's primary raw material. Any purchase above the quota would be subject to a 25% tariff. To date, the Company has been able to import wire rod within the provisional quotas and has not been subject to the additional tariff.

In conjunction with the provisional safeguards, the Canadian government has directed the Canadian International Trade Tribunal ("CITT") to conduct an inquiry into and report on the importation of those seven classes of steel goods noted above. The purpose of this inquiry is to determine whether any of the above-mentioned goods imported into Canada are considered to cause serious injury or threat to Canadian producers of like or directly competitive goods.

Imports from the United States, Israel and other CIFTA beneficiaries, such as Chile are excluded from the Tribunal's inquiry. If it makes an affirmative determination for any class of goods, the Tribunal is being directed to recommend the most appropriate remedy to address, over a period of three years, in accordance with Canada's rights and obligations under international trade agreements.

A report, including any recommendations is scheduled to be completed by April 3, 2019. The Company has participated in the CITT review. Tree Island at this time cannot determine whether the CITT review will have an impact on Tree Island's Canadian raw material supply chain and purchasing programs.

4.2.4 U.S. Trade Case Against Carbon and Certain Alloy Steel Wire Rod

On March 28, 2017 a petition was submitted to the U.S. Department of Commerce and U.S. International Trade Commission initiating a trade case against imports of wire rod into the U.S. from ten countries on behalf of U.S. domestic producer plaintiffs Gerdau, Nucor, Keystone and Charter Steel. The countries investigated were Belarus, Italy, Russia, South Africa, South Korea, Spain, Turkey, Ukraine, United Arab Emirates and the United Kingdom. The U.S. International Trade Commission confirmed the final determination on import wire rod duties against all ten countries as of May 1, 2018.

Tree Island does not purchase any rod for its U.S. operations from those countries under investigation.

4.2.5 United States Mexico Canada Agreement ("USMCA")

The USMCA is a pending updated free trade agreement between Canada, Mexico, and the United States from the 2017-2018 renegotiation of NAFTA (North American Free Trade Agreement) by its member states. The three countries formally agreed to terms with final ratification and implementation pending.

The Company cannot assess at this time whether the finalization of the USMCA will have a negative or positive effect on the Company's ability to source or sell its products into the U.S. market.

5 RESULTS FROM OPERATIONS

(\$'000 unless otherwise stated)

	Three Months Ended December 31,		Years Ended December 31,		
	2018	2017	2018	2017	2016
Revenue	44,882	54,561	235,306	234,705	231,253
Cost of sales	(40,293)	(51,266)	(205,977)	(213,223)	(190,521)
Depreciation	(903)	(843)	(3,492)	(3,291)	(3,319)
Gross profit	3,686	2,452	25,837	18,191	37,413
Selling, general and administrative expenses	(3,932)	(1,482)	(16,646)	(13,899)	(19,388)
Operating income	(246)	970	9,191	4,292	18,025
Foreign exchange gain (loss)	408	119	706	(582)	(375)
Gain (loss) on property, plant and equipment	(666)	68	(664)	(47)	12
Other expenses	(799)	(635)	(903)	(635)	(57)
Changes in financial liabilities recognized at fair value	22	(420)	(67)	84	149
Financing expenses	(1,008)	(773)	(3,500)	(2,967)	(2,753)
Income (loss) before income taxes	(2,289)	(671)	4,763	145	15,001
Current income tax (expense) recovery	(21)	-	(332)	(2)	(504)
Deferred income tax (expense) recovery	(24)	(1,303)	(1,838)	(1,781)	(929)
Net income (loss)	(2,334)	(1,974)	2,593	(1,638)	13,568
Operating income (loss)	(246)	970	9,191	4,292	18,025
Add back depreciation	903	843	3,492	3,291	3,319
Foreign exchange gain (loss)	408	119	706	(582)	(375)
EBITDA ¹	1,065	1,932	13,389	7,001	20,969
Net income per share	(0.08)	(0.07)	0.09	(0.05)	0.44
Dividends per share	0.02	0.02	0.08	0.08	0.07

Financial position as at:	December 31,		
	2018	2017	2016
Total assets	158,449	133,681	137,455
Total non-current financial liabilities	21,928	18,356	19,090

6 COMPARISON OF RESULTS FOR THE THREE MONTHS ENDED December 31, 2018 AND 2017

(\$'000 unless otherwise stated)	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
SALES	44,882	54,561	(9,679)	(17.7%)

Revenue for the quarter decreased by 17.7% primarily due to a combination of the U.S. Section 232 import tariffs impacting our volumes shipped to the U.S., particularly in our Industrial segment, and seasonal weather conditions affecting the construction business. Despite these challenges, revenues grew in the Commercial markets.

¹ See definition of EBITDA in Section 2 NON-IFRS MEASURES

Revenue by Market Segment

(\$'000 unless otherwise stated)

	Three Months Ended December 31,					
	2018		2017		Variance	
	Revenue	% of Total	Revenue	% of Total	Amount	%
Industrial	15,156	33.8%	21,400	39.2%	(6,244)	(29.2%)
Commercial	13,953	31.1%	10,417	19.1%	3,536	33.9%
Agricultural	3,387	7.5%	4,462	8.2%	(1,075)	(24.1%)
Residential	12,386	27.6%	18,282	33.5%	(5,896)	(32.3%)
Total revenue	44,882	100.0%	54,561	100.0%	(9,679)	(17.7%)

Revenue by Location

(\$'000 unless otherwise stated)

	Three Months Ended December 31,					
	2018		2017		Variance	
	Revenue	% of Total	Revenue	% of Total	Amount	%
United States	28,407	63.3%	35,540	65.1%	(7,133)	(20.1%)
Canada	14,992	33.4%	17,739	32.5%	(2,747)	(15.5%)
International	1,483	3.3%	1,282	2.4%	201	15.7%
Total	44,882	100.0%	54,561	100.0%	(9,679)	(17.7%)
Average C\$/US\$	1.3178		1.2711			

(\$'000 unless otherwise stated)	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
COST OF SALES	40,293	51,266	10,973	21.4%

The cost of goods sold decreased when compared to the same period last year, which is reflective of the re-balancing in production levels to match lower volumes and our on-going commitment to cost management.

(\$'000 unless otherwise stated)	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
GROSS PROFIT	3,686	2,452	1,234	50.3%

Gross profit for the three months amounted to \$3.7 million versus \$2.5 million during the same period last year. The increase in gross profit is primarily a result of improved profitability through better product mix and from price increases implemented to offset the increase in raw material input costs and tariffs.

(\$'000 unless otherwise stated)	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
SG&A EXPENSES	3,932	1,482	(2,450)	(165.3%)

Excluding the reversal of an accrual of \$2.3 million for compensation related items in the prior year, SG&A expenses were consistent with the prior year.

(\$'000 unless otherwise stated)	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
EBITDA	1,065	1,932	(867)	(44.9%)

EBITDA earned for the quarter is inclusive of a \$408k foreign exchange gain (compared to a \$119k gain in 2017). The decrease in EBITDA is primarily a result of lower volume to our U.S. markets in the quarter impacted by Section 232 tariffs as well as seasonal weather conditions for construction.

<i>(\$'000 unless otherwise stated)</i>	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
FINANCING EXPENSES	1,008	773	(235)	(30.4%)

Financing expenses increased mainly due to higher interest rates on the senior credit facility and increased borrowings on the senior credit facility. The increase in the facility was due to higher levels of raw material and zinc purchases during the year.

Financing Expense

(\$'000 unless otherwise stated)

	Three Months Ended December 31,			
	<u>2018</u>	<u>2017</u>	<u>Variance Fav / (Unfav)</u>	
			<u>Amount</u>	<u>%</u>
Non-cash financing expenses	226	247	21	8.5%
Interest on senior credit facility	460	291	(169)	(58.1%)
Other interest and financing costs	313	223	(90)	(40.4%)
Deferred financing costs	9	12	3	25.0%
Total financing expenses	1,008	773	(235)	(30.4%)

<i>(\$'000 unless otherwise stated)</i>	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
FOREIGN EXCHANGE	408	119	289	242.9%

Our Canadian operation, whose functional currency is the Canadian dollar, has a portion of its assets, liabilities, sales and expenses denominated in currencies other than the Canadian dollar, in particular the U.S. dollar. With raw material costs being denominated in U.S. dollars, having a significant portion of our sales also being denominated in U.S. dollars creates a natural partial hedge. Foreign currency forward contracts are used to manage a portion of the remaining currency risk. Foreign exchange gains and losses are unpredictable in nature and therefore can vary significantly over time. As at December 31, 2018, the Company did not have any U.S. dollar currency forward contracts outstanding.

<i>(\$'000 unless otherwise stated)</i>	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
INCOME TAX (EXPENSE)	(45)	(1,303)	1,258	96.5%

The income tax expense for Q4 2018 is based on the Canadian statutory rate of 27%, with adjustments for permanent differences between accounting and taxable income.

The income tax expense in 2017 is the result of increase in the deferred taxes for the year mainly due to accelerated depreciation taken on fixed asset for tax versus for book, reduction in deferred tax asset due to utilization of the loss carry forward and as a result of the reduction in the corporate tax rate for our US operations as a result of the tax reform which reduces the benefit of the deferred tax asset booked in future years.

<i>(\$'000 unless otherwise stated)</i>	Q4 2018	Q4 2017	Variance Fav/(Unfav)	
NET INCOME (LOSS)	(2,334)	(1,974)	(360)	(18.2%)

The net loss before income taxes in 2018 was loss compared to 2017 due to lower SG&A expenses in the prior year from the reversal of an accrual for compensation related items offset by a higher deferred tax expense.

7 COMPARISON OF RESULTS FOR THE YEAR ENDED DECEMBER 31, 2018 AND 2017

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
SALES	235,306	234,705	601	0.3%

Revenues for 2018 was in-line with the prior year. The price increases implemented over the course of the year and our focus on selling higher margin products helped to mitigate the impact of lower volumes for the year from our U.S. customers in the Industrial market due to the steel import tariffs.

Revenue by Market Segment

(\$'000 unless otherwise stated)

	Years Ended December 31,					
	2018		2017		Variance	
	<u>Revenue</u>	<u>% of Total</u>	<u>Revenue</u>	<u>% of Total</u>	<u>Amount</u>	<u>%</u>
Industrial	79,295	33.7%	84,379	36.0%	(5,084)	(6.0%)
Commercial	54,375	23.1%	44,753	19.1%	9,622	21.5%
Agricultural	28,044	11.9%	28,886	12.3%	(842)	(2.9%)
Residential	73,592	31.3%	76,687	32.7%	(3,095)	(4.0%)
Total revenue	235,306	100.0%	234,705	100.0%	601	0.3%

Revenues generated in the U.S. and in Canada improved over the prior year on account of higher prices offset by lower volumes as noted above.

Revenue by Location

(\$'000 unless otherwise stated)

	Years Ended December 31 ,					
	2018		2017		Variance	
	<u>Revenue</u>	<u>% of Total</u>	<u>Revenue</u>	<u>% of Total</u>	<u>Amount</u>	<u>%</u>
United States	148,410	63.1%	148,336	63.2%	74	0.0%
Canada	80,381	34.1%	78,269	33.3%	2,112	2.7%
International	6,515	2.8%	8,100	3.5%	(1,585)	(19.6%)
Total	235,306	100.0%	234,705	100.0%	601	0.3%

Average C\$/US\$ 1.2925 1.2984

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
COST OF SALES	205,977	213,223	7,246	3.4%

The cost of goods sold decreased when compared to last year, which is reflective of the re-balancing in production levels to match lower volumes and our on-going commitment to cost management.

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
GROSS PROFIT	25,837	18,191	7,646	42.0%

Our focus on operational efficiency and cost management, improved profitability from product mix, and prices increases on finished products were key factors to our gross profit increasing from \$18.2 million in 2017 to \$25.8 million in 2018. The gross profit margin for the year was 11.0% compared to 7.8% the year prior.

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
SG&A EXPENSES	16,646	13,899	(2,747)	(19.8%)

Excluding the reversal of an accrual of \$2.3 million for compensation related items in the prior year, SG&A expenses were consistent with the prior year.

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
EBITDA	13,389	7,001	6,388	91.2%

EBITDA for the full year is inclusive of a foreign exchange gain of \$706k (loss of \$582k in 2017). The increase in EBITDA is primarily a result of improved gross profit margins over the course of the year, our focus on selling higher margin products, and our continual focus on operational excellence; offset by the impact of lower volumes for the year.

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
FINANCING EXPENSES	3,500	2,967	(533)	(18.0%)

Financing expenses increased mainly due to higher interest rates on the senior credit facility and increased borrowings on the senior credit facility from the higher purchases of raw material and other inventories in the year.

Financing Expense

(\$'000 unless otherwise stated)

	Years Ended December 31,			
	<u>2018</u>	<u>2017</u>	<u>Variance Fav / (Unfav)</u>	
			<u>Amount</u>	<u>%</u>
Non-cash financing expenses	931	1,074	143	13.3%
Interest on senior credit facility	1,533	1,056	(477)	(45.2%)
Other interest and financing costs	946	789	(157)	(19.9%)
Deferred financing costs	90	48	(42)	(87.5%)
Total financing expenses	3,500	2,967	(533)	(18.0%)

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
FOREIGN EXCHANGE	706	(582)	1,288	221.3%

Our Canadian operation, whose functional currency is the Canadian dollar, has a portion of its assets, liabilities, sales and expenses denominated in currencies other than the Canadian dollar, in particular the U.S. dollar. With raw material costs being denominated in U.S. dollars, having a significant portion of our sales also being denominated in U.S. dollars creates a natural partial hedge. Foreign currency forward contracts are used to manage a portion of the remaining currency risk. Foreign exchange gains and losses are unpredictable in nature and therefore can vary significantly over time. As at December 31, 2018, the Company did not have any U.S. dollar currency forward contracts outstanding.

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
INCOME TAX (EXPENSE)	(2,170)	(1,783)	(387)	(21.7%)

The income tax expense for 2018 is based on the Canadian statutory rate of 27%, with adjustments for permanent differences between accounting and taxable income.

<i>(\$'000 unless otherwise stated)</i>	<u>YTD 2018</u>	<u>YTD 2017</u>	<u>Variance Fav/(Unfav)</u>	
NET INCOME (LOSS)	2,593	(1,638)	4,231	258.3%

Net income improved appreciably over last year from improved gross profit margins, improved product mix and focus on cost management.

8 FINANCIAL CONDITION AND LIQUIDITY

8.1 WORKING CAPITAL

A summary of the composition of our working capital as at December 31, 2018 compared to 2017 is provided below:

Working Capital

(\$'000 unless otherwise stated)

	As at December 31,	
	<u>2018</u>	<u>2017</u>
Cash	1,277	1,651
Accounts receivable	24,128	26,147
Inventories	81,619	59,992
Other current assets	4,013	3,569
Total current assets	<u>111,037</u>	<u>91,359</u>
Senior credit facility	(49,797)	(33,468)
Accounts payable and accrued liabilities	(22,017)	(18,272)
Dividends payable	(584)	(593)
Other current liabilities	(517)	(178)
Current portion of long term debt	(4,980)	(3,545)
Total current liabilities	<u>(77,895)</u>	<u>(56,056)</u>
Net working capital	<u>33,142</u>	<u>35,303</u>

Our business requires an ongoing investment in working capital, comprised primarily of accounts receivable and inventories, financed primarily by credit in the form of our Senior Credit Facility and accounts payable and accrued liabilities. Our largest investment in working capital is in our inventories. We have arrangements with our key suppliers to provide us with financing or trade credit for the purchase of the raw materials needed for our operations.

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. The construction and agricultural markets are seasonal in nature. As a result, sales and working capital requirements may be higher in the first three quarters when demand is historically highest.

Accounts receivable as at December 31, 2018 was lower than at the same period last year, reflecting the decrease in sales in Q4 2018 compared to the same period in the prior year. Inventories levels were higher as at December 31, 2018 when compared to the same period in 2017 as a result of higher levels of raw materials and other inventories on hand resulting from the decline in volumes to our U.S. markets on the imposition of Section 232 tariffs.

The increase in accounts payable and accrued liabilities is reflective of the increase in raw material costs relative to last year and reflective in part, the difference in the timing of payments made and expenses incurred.

Our objective for managing the investment in working capital is to maximize the turnover of productive current assets, being accounts receivable and inventories. Our goal is to keep utilization of our Senior Credit Facility as low as practicable to maintain borrowing capacity for when it is needed and to reduce ongoing interest costs. We also work with our key vendors to use vendor credit when available on advantageous terms.

We manage our inventories with an emphasis on a continuous inflow of raw materials to meet our production needs balanced with strategic purchases, barring unforeseen events such as the Section 232 tariffs impacting potential end markets. We have also established processes to regularly adjust the production levels of finished goods stocked in our warehouses so that we can both satisfy customer needs, growth requirements and meet our objective of minimizing inventories on hand.

We manage our accounts receivable and the related credit risk by focusing on well-established customers with favourable credit profiles. The credit worthiness of customers is assessed using credit scores supplied by a third party and through direct monitoring of their financial well-being on a continual basis. We have established guidelines for customer credit limits and when thresholds in these areas are reached, appropriate precautions are taken to improve collectability or limit increasing credit exposure. We maintain provisions for potential credit losses (allowance for doubtful accounts) and such losses to date have been within our expectations.

8.2 CASH FLOW

Cash Flow

(\$'000 unless otherwise stated)

	Three Months Ended December 31,		Years Ended December 31,	
	2018	2017	2018	2017
Cash provided by operating activities	660	1,417	12,857	5,688
Working capital adjustments	259	11,015	(16,758)	9,377
Net cash provided by (used in) operating activities	919	12,432	(3,901)	15,065
Net cash used in investing activities	(2,942)	(862)	(8,507)	(6,362)
Advance on (repayment of) senior term loans	(482)	(436)	2,587	(1,749)
Repayment of long-term debt	(481)	(460)	(1,873)	(2,542)
Other payables	686	148	1,127	144
Interest paid	(731)	(517)	(2,393)	(1,805)
Deferred financing expenses	-	-	(183)	-
Advance on (repayment of) senior revolving facility	2,598	(6,971)	16,328	4,522
Dividend payment	(585)	(611)	(2,356)	(2,462)
Share buyback	(202)	(2,500)	(1,262)	(4,446)
Net cash provided by (used in) financing activities	803	(11,347)	11,975	(8,338)
Exchange rate changes on foreign cash balances	41	(8)	59	(65)
Increase (decrease) in cash balances	(1,179)	215	(374)	300

For the three months ended December 31, 2018, the net cash used in investing activities increased which was for capital maintenance activities and capital investments which are further described in Section 9.

For the year, the decrease in net cash provided by operating activities is a direct result of additional working capital required when compared to the prior year. The net cash used in investing activities was from capital investments

which are further described in Section 9. The net cash provided by financing activities was mainly due to advances on the senior revolving facility when compared to the prior year.

8.3 SENIOR CREDIT FACILITY

On July 1, 2018, the Company renewed its senior secured committed banking facility, now maturing in June of 2023, which enables the Company to borrow up to \$80.0 million in Canadian and/or U.S. funds. Interest payable on funds borrowed in Canadian currency is at variable rates based on the Canadian Dollar Offered Rate (“CDOR”) for Canadian dollar banker’s acceptance. Interest payable on funds borrowed in U.S. currency is at variable rates based on the London Interbank Offered Rate (“LIBOR”) for U.S. dollar deposits. For the revolving facility, up to \$60 million may be borrowed at any time in Canadian and/or U.S. dollars with the amount advanced under the revolving facility limited to a defined percentage of inventories, accounts receivable, machinery and equipment, and real estate, less certain reserves. In addition, up to \$20 million may be borrowed as term debt, in Canadian and/or U.S. dollars for financing existing machinery and equipment and future capital expenditures.

The existing term debts applied against the Senior Credit Facility was incorporated into a single term loan of \$10 million, denominated in Canadian dollars on July 1, 2018, referred to as “Fixed Asset Term Loan”. An additional \$10 million is available to finance future capital expenditures, to be denominated in either Canadian or U.S. dollars and referred to as “Capex Term Loans”. On September 24, 2018, US\$2.9 million was applied against the “Capex Term Loan” for financing a new welded wire mesh machine in our U.S. Operations.

The Senior Credit Facility is secured by a first charge over Tree Island's assets supported by the appropriate guarantees, pledges and assignments, and requires that certain covenants be met by Tree Island. The Senior Credit Facility has defined covenants, the primary one being based on the remaining funds within the Senior Credit Facility that is available (“Availability Test”). Only if this amount falls below a certain threshold, then other covenants, which include a defined fixed charge coverage ratio, are tested. In addition, there are other restrictive covenants that limit the discretion of management with respect to certain business matters.

As at December 31, 2018 the availability was in excess of the Availability Test and the Company was in compliance with its covenants on the Senior Credit Facility.

8.4 LONG TERM DEBT AGREEMENT

On June 11, 2012, Tree Island entered into a Second Amendment to the long-term debt agreement (“Agreement”). Under the terms of this Agreement, the total principal debt amount of approximately US\$15.8 million is to be repaid monthly over a ten year amortization period, of which \$7.4 million is outstanding as at December 31, 2018. Interest, which began accruing in June 2017, is non-compounding. The interest owed is payable over a four year period beginning June 2024 (see Note 9 in the consolidated financial statements).

9 CAPITAL EXPENDITURES AND CAPACITY

For the fourth quarter and full year ended December 31, 2018, we made capital expenditures of \$2.9 million and \$8.5 million, respectively. These expenditures were for capital maintenance activities and new manufacturing equipment. As noted in section 10 of this MD&A there are a further \$0.5 million in capital equipment commitments in 2019, which represent the final balances payable for the capital equipment delivered in 2018.

10 CONTRACTUAL OBLIGATIONS AND COMMITMENTS

As of December 31, 2018, we were committed to the contracts, operating leases and debt repayments (including scheduled interest payments on interest bearing debt) set out below, which will be financed through working capital and our Senior Credit Facility.

The production materials include raw materials, such as wire rod and zinc, and finished goods. The raw materials, wire rod and zinc, are used in the day-to-day operations of our manufacturing facilities and are in the normal course of our business activities. Finished goods are purchased for resale without further processing and are also in the normal course of our business activities. All committed production materials are to be delivered prior to the end of Q2 2019.

From time to time, we make investments to update, replace or make additions to our existing capital assets, which includes, but is not limited to, the buildings we occupy and capital equipment. These investments are in the normal course of our business activity. All capital asset commitments amounts are expected to be paid by the end of Q1 2019.

We have leases for facilities and equipment that are considered to be operating leases for accounting purposes and as such are not recorded on the consolidated statement of financial position.

From time to time, the Company enters into U.S. dollar currency forward contracts for periods consistent with a portion of U.S. dollar currency transaction exposures, generally from one to three months. These are not designated as cash flow, fair value or net investment hedges. As of December 31, 2018, the Company did not have any U.S. dollar currency forward contracts outstanding.

Contractual Obligations and Commitments

(\$'000 unless otherwise stated)

	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>Thereafter</u>	<u>Total</u>
Production materials	28,375	-	-	-	-	-	28,375
Machinery and equipment	533	-	-	-	-	-	533
Operating leases	3,346	3,247	3,214	3,070	2,010	16,282	31,169
Total commitments	<u>32,254</u>	<u>3,247</u>	<u>3,214</u>	<u>3,070</u>	<u>2,010</u>	<u>16,282</u>	<u>60,077</u>
Senior revolving facility	49,797	-	-	-	-	-	49,797
AP and accrued liabilities	22,017	-	-	-	-	-	22,017
Other current liabilities	346	-	-	-	-	-	346
Dividends	584	-	-	-	-	-	584
Senior term loans	1,986	1,986	1,986	1,986	1,986	3,405	13,335
Long-term debt	2,994	1,571	1,457	491	-	5,103	11,616
Total financial liabilities	<u>77,724</u>	<u>3,557</u>	<u>3,443</u>	<u>2,477</u>	<u>1,986</u>	<u>8,508</u>	<u>97,695</u>
Total obligations and commitments	<u>109,978</u>	<u>6,804</u>	<u>6,657</u>	<u>5,547</u>	<u>3,996</u>	<u>24,790</u>	<u>157,772</u>

11 SUMMARY OF QUARTERLY FINANCIAL RESULTS

The table below provides selected quarterly financial information for the eight most recent fiscal quarters to December 31, 2018. Sales volume in the fourth quarter of the year has traditionally been the lowest in the year due to the seasonality of our business and the markets we sell to. Quarter-over-quarter results may also be impacted by unusual or infrequently occurring items.

Summary of Quarterly Financial Results

(\$'000 unless otherwise stated)

	Dec 31, <u>2018</u>	Sep 30, <u>2018</u>	Jun 30, <u>2018</u>	Mar 31, <u>2018</u>	Dec 31, <u>2017</u>	Sep 30, <u>2017</u>	Jun 30, <u>2017</u>	Mar 31, <u>2017</u>
Revenue	44,882	55,846	68,087	66,491	54,561	55,643	61,455	63,040
Gross profit	3,686	6,936	8,509	6,706	2,452	2,299	5,943	7,495
Foreign exchange gain (loss)	408	(77)	256	119	119	(737)	(61)	97
EBITDA	1,065	3,383	5,451	3,490	1,932	(1,496)	2,375	4,187
Net income (loss)	(2,334)	1,030	2,792	1,105	(1,974)	(2,152)	735	1,750
Net income (loss) per unit - basic	(0.08)	0.03	0.09	0.04	(0.07)	(0.07)	0.04	0.06

Commentary:

- The rapid rise in raw material costs had a negative impact on the gross profit and EBITDA for most of 2017.
- The average prices of finished good products increased month-over-month to counter inflationary cost of raw materials during 2018.
- The imposition of Section 232 in June 2018 negatively impacted our sales to the U.S. market particularly in the Industrial market in the third and fourth quarter of 2018.

These financial results are not necessarily indicative of results for any future period and should not be relied upon to predict future performance.

12 ACCOUNTING POLICIES AND STATEMENTS

Certain of our accounting policies involve critical accounting estimates that require us to make subjective or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts could be reported under differing conditions or using different assumptions. We evaluate these estimates and assumptions regularly.

Our significant accounting policies are described in Note 3 of the December 31, 2018 Consolidated Financial Statements and in the Annual Information Form for the year ended December 31, 2018.

12.1 CRITICAL ACCOUNTING ESTIMATES

The areas that we consider to have critical accounting estimates are: inventory valuation, allowance for doubtful accounts, property, plant and equipment, and income taxes. These critical estimates and the judgments involved are discussed further in Note 3 to the audited Consolidated Financial Statements for December 31, 2018.

13 RELATED PARTY TRANSACTIONS

13.1 TRANSACTIONS WITH ASSOCIATED COMPANIES

The Futura Corporation ("Futura") is considered to be a related party to the Company because of its share ownership interest and the fact that Mr. Doman, the sole shareholder and president of Futura, and Mr. Rosenfeld, the Executive Vice President of Futura, sit on the Board of Directors.

Based on Tree Island Steel's outstanding Shares as at February 20, 2019, Futura owns 30.2% of the fully diluted Shares of the Company.

In addition, Mr. Doman is Chairman and CEO of CanWel Building Materials Group Ltd. (“CanWel”). For the twelve months ended December 31, 2018, Tree Island sold, net of rebates, approximately \$3.6 million (\$2.9 million in 2017) of goods to CanWel and trade accounts receivable owing from CanWel as at December 31, 2018 is approximately \$0.1 million (approximately \$0.1 million in 2017). Outstanding trade accounts receivable from CanWel at period end are unsecured, interest free and settlement occurs in cash.

13.2 TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL

Included in the definition of key management for purposes of disclosure of related party transactions are members of Board of Directors and officers of Tree Island Steel. Amounts for key management personnel for the year ended December 31, 2018 was approximately and \$2.9 million respectively (\$2.7 million respectively in 2017) which includes wages, salaries and social security contributions, paid annual and sick leave, vehicle costs and bonuses and severance amount payable to an officer. It also includes directors’ fees paid to members of the Board.

14 RISKS AND UNCERTAINTIES

Investment in Tree Island Steel is subject to a number of risks. Our income is dependent upon the wire products business, which is susceptible to a number of risks. Risks pertaining to current economic conditions are discussed in the section above under the heading “2018 Business Overview and Development”. A detailed discussion of our significant business risks is provided in the 2018 Annual Information Form under the heading “Risk Factors” which can be found at www.sedar.com.

15 DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for designing disclosure controls and procedures that (a) provide reasonable assurance that material information required to be disclosed by us is accumulated and communicated to management to allow timely decisions regarding required disclosure; and (b) ensure that information required to be disclosed by us is recorded, processed, summarized, and reported within the time periods specified in applicable securities legislation.

Our management is responsible for designing, establishing, and maintaining an adequate system of internal control over financial reporting. Our internal control system was designed based on the 2013 Internal Control – Integrated Framework (“2013 COSO Framework”) published by the Committee of Sponsoring Organizations of the Treadway Commission to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes, in accordance with IFRS.

Our management, with the participation of the Chief Executive Officer and the Chief Financial Officer, has conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2018 based on the 2013 COSO Framework. Based on that evaluation, management concluded that our internal control over financial reporting, as defined by National Instrument 52-109, Certification of Disclosure in Issuers’ Annual and Interim Filings, is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS.

Our Chief Executive Officer and Chief Financial Officer certified the appropriateness of the financial disclosures in the annual financial report together with the other financial information included in the annual filings for the year ended December 31, 2018. These executives also certified that they are responsible for the design of disclosure controls and procedures and internal control over financial reporting.

Under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, we have evaluated changes in internal control over financial reporting that occurred during the

fiscal year ended and found no change that has materially affected, or is reasonably likely to materially affect, internal control over financial reporting.

The Company's Board of Directors and Audit Committee reviewed and approved the December 31, 2018 consolidated financial statements and this MD&A prior to its release.

CONSOLIDATED FINANCIAL STATEMENTS

MANAGEMENT'S STATEMENT OF RESPONSIBILITY

The accompanying consolidated financial statements are the responsibility of management and have been reviewed and approved by the Board of Directors. The consolidated financial statements have been prepared by management, in accordance with the International Financial Reporting Standards and, where appropriate, reflect management's best estimates and judgements. Management has also prepared financial and all other information in the annual report and has ensured that this information is consistent with the consolidated financial statements.

The Company maintains appropriate systems of internal control, policies and procedures, which provide management with reasonable assurance that assets are safeguarded and the financial records are reliable and form a proper basis for preparation of the consolidated financial statements.

The Board of Directors ensures that management fulfills its responsibilities for financial reporting and internal control through an Audit Committee. This committee reviews the consolidated financial statements and reports to the Directors. The auditors have full and direct access to the Audit Committee.

The consolidated financial statements have been independently audited by KPMG LLP, in accordance with Canadian generally accepted auditing standards. Their report below expresses their opinion on the consolidated financial statements of the Company.

Dale R. Maclean
Director, President and Chief Executive Officer



KPMG LLP
PO Box 10426 777 Dunsmuir Street
Vancouver BC V7Y 1K3
Canada
Telephone (604) 691-3000
Fax (604) 691-3031

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Tree Island Steel Ltd.,

Opinion

We have audited the accompanying consolidated financial statements of Tree Island Steel Ltd. (the Company), which comprise:

- the consolidated statement of financial position as at December 31, 2018
- the consolidated statement of operations for the year then ended
- the consolidated statement of comprehensive income (loss) for the year then ended
- the consolidated statement of shareholders' equity for the year then ended
- the consolidated statement of cash flows for the year then ended
- and notes to the consolidated financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Comparative information

The financial statements of Tree Island Steel Ltd. as at and for the year ended December 31, 2017, excluding the adjustment of \$ Nil described in Note 3, were audited by another auditor who expressed an unmodified opinion on those financial statements on February 22, 2018.

As part of our audit of the financial statements for the year ended December 31, 2018, we also audited the adjustment of \$ Nil described in Note 3. In our opinion, the adjustment of \$ Nil described in Note 3 is appropriate and has been properly applied.

Other than with respect to the adjustment of \$ Nil described in Note 3, we were not engaged to audit, review or apply any procedures to the financial statements as at and for the year ended December 31, 2017. Accordingly, we do not express an opinion or any other form of assurance on those financial statements taken as a whole.



Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the “***Auditors’ Responsibilities for the Audit of the Financial Statements***” section of our auditors’ report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information

Management is responsible for the other information. Other information comprises:

- Management’s Discussion and Analysis filed with the relevant Canadian Securities Commissions.
- Information, other than the financial statements and the auditors’ report thereon, included in a document likely to be entitled “Annual Report”.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit and remain alert for indications that the other information appears to be materially misstated.

We obtained the Management’s Discussion and Analysis filed with the relevant Canadian Securities Commissions as at the date of this auditors’ report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors’ report.

We have nothing to report in this regard.

Information, other than the financial statements and the auditors’ report thereon, included in a document likely to be entitled “Annual Report” is expected to be made available to us after the date of this auditors’ report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance



Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgement and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to



events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair representation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

KPMG LLP (signed)

Chartered Professional Accountants

The engagement partner on the audit resulting in this auditors' report is Andrew James
Vancouver, Canada
February 20, 2019

CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Cash	1,277	1,651
Accounts receivable (Notes 5, 12.1)	24,128	26,147
Inventories (Note 6)	81,619	59,992
Prepaid and other current assets	4,013	3,421
Income taxes recoverable	-	148
Current assets	111,037	91,359
Property, plant and equipment (Notes 7, 18.2)	47,230	41,690
Deferred income tax asset (Note 14.2)	-	563
Other non-current assets	182	69
Total assets	158,449	133,681
Senior revolving facility (Note 8.1)	49,797	33,468
Accounts payable and accrued liabilities	22,017	18,272
Income taxes payable	171	-
Other current liabilities	346	178
Dividends payable	584	593
Current portion of long-term debt and senior term loans (Notes 8.2, 9)	4,980	3,545
Current liabilities	77,895	56,056
Senior term loans (Note 8.2)	11,349	8,808
Long-term debt (Note 9)	4,922	6,381
Other non-current liabilities	2,426	1,186
Deferred income tax liability (Note 14.2)	3,231	1,981
Total liabilities	99,823	74,412
Shareholders' equity	58,626	59,269
Total liabilities and shareholders' equity	158,449	133,681

See accompanying Notes to the Consolidated Financial Statements

Approved on behalf of Tree Island Steel.

[Signed]
"Amar S. Doman"
Chairman of the Board of Directors

[Signed]
"Dale R. Maclean"
Director, President and Chief Executive Officer

CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

CONSOLIDATED STATEMENTS OF OPERATIONS

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Sales (Notes 5, 12.1, 19)	235,306	234,705
Cost of sales (Note 6)	(205,977)	(213,223)
Depreciation	(3,492)	(3,291)
Gross profit	25,837	18,191
Selling, general and administrative expenses	(16,646)	(13,899)
Operating income	9,191	4,292
Foreign exchange gain (loss)	706	(582)
Gain (loss) on sale of property, plant and equipment	(664)	(47)
Other expenses	(903)	(635)
Changes in financial liabilities at fair value	(67)	84
Financing expenses (Note 10)	(3,500)	(2,967)
Income before income taxes	4,763	145
Current income tax expense (Note 14)	(332)	(2)
Deferred income tax expense (Note 14)	(1,838)	(1,781)
Net income (loss)	2,593	(1,638)
Net income (loss) per share (Note 17)	0.09	(0.05)
Dividends per share	0.08	0.08
Weighted average number of shares (Note 17)	29,411,890	30,623,785

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Net income (loss) for the year	2,593	(1,638)
Unrealized gain (loss) on foreign exchange translation	373	(786)
Comprehensive income (loss)	2,966	(2,424)

See accompanying Notes to the Consolidated Financial Statements

CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(\$'000 unless otherwise stated)

	Shareholders' Capital (Note 11)	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance as at December 31, 2017	225,977	(163,600)	(3,108)	59,269
Repurchase of shares	(1,262)	-	-	(1,262)
Net income (loss)	-	2,593	-	2,593
Dividends	-	(2,347)	-	(2,347)
Other comprehensive income (loss)	-	-	373	373
Balance as at December 31, 2018	224,715	(163,354)	(2,735)	58,626
Balance as at December 31, 2016	230,423	(159,528)	(2,322)	68,573
Repurchase of shares	(4,446)	-	-	(4,446)
Net income	-	(1,638)	-	(1,638)
Dividends	-	(2,434)	-	(2,434)
Other comprehensive income (loss)	-	-	(786)	(786)
Balance as at December 31, 2017	225,977	(163,600)	(3,108)	59,269

See accompanying Notes to the Consolidated Financial Statements

CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

CONSOLIDATED STATEMENTS OF CASH FLOWS

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Net income (loss)	2,593	(1,638)
Depreciation	3,492	3,291
Changes in financial liabilities recognized at fair value	67	(84)
Loss on sale of property, plant and equipment	664	47
Net financing costs	3,500	2,967
Deferred income tax expense	1,838	1,781
Exchange revaluation of foreign denominated debt (Note 9)	703	(676)
Working capital adjustments		
Accounts receivable	2,020	(1,685)
Inventories	(21,674)	7,295
Accounts payable and accrued liabilities	3,697	3,630
Prepaid expenses	(573)	450
Income and other taxes	332	(418)
Other	(560)	105
Net cash provided by (used in) operating activities	(3,901)	15,065
Proceeds on sale of property, plant and equipment	33	25
Government incentives	-	193
Purchase of property, plant and equipment	(8,540)	(6,580)
Net cash used in investing activities	(8,507)	(6,362)
Term loans – advances (repayment), net (Note 8.2)	2,587	(1,749)
Repayment of long-term debt	(1,873)	(2,542)
Other financing liabilities	1,127	144
Interest paid	(2,393)	(1,805)
Deferred financing fees	(183)	-
Increase of senior revolving facility	16,328	4,522
Dividend paid	(2,356)	(2,462)
Repurchase of common shares	(1,262)	(4,446)
Net cash provided by (used in) financing activities	11,975	(8,338)
Effect of exchange rate change on cash	59	(65)
Increase (decrease) in cash	(374)	300
Cash - beginning of year	1,651	1,351
Cash - end of year	1,277	1,651

See accompanying Notes to the Consolidated Financial Statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

1 NATURE OF BUSINESS

These consolidated financial statements of Tree Island Steel ("Tree Island Steel" or the "Company") for the years ended December 31, 2018 and 2017 were authorized for issue in accordance with a resolution of the Board of Directors on February 20, 2019.

Tree Island Steel is the successor to Tree Island Income Fund and was incorporated under the laws of Canada on August 2, 2012 to affect the conversion from an income trust to a corporate entity. The units of Tree Island Wire Income Fund were converted into common shares of the Company ("Shares") upon conversion. The Company is headquartered at 3933 Boundary Road, Richmond, British Columbia, Canada and the Shares are publicly traded on the Toronto Stock Exchange ("TSX") under the symbol TSL.

Tree Island Steel owns 100% of the shares of Tree Island Industries ("TI Canada") (collectively "Tree Island"). TI Canada supplies a diverse range of steel wire and fabricated steel wire products to customers in Canada, the United States, and internationally.

2 BASIS OF PREPARATION

2.1 BASIS OF PREPARATION

The consolidated financial statements as at and for the year ended December 31, 2018 have been prepared in accordance with International Financial Reporting Standards ("IFRS").

These consolidated financial statements have been prepared on a historical cost basis except for certain financial instruments categorized as fair value through profit or loss. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting.

2.2 BASIS OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company, TI Canada, and TI Canada's wholly-owned subsidiaries, Tree Island Wire Holdings. ("TIWH") and Tree Island Wire. ("TI USA"). Intercompany accounts and transactions have been eliminated on consolidation.

2.3 FUNCTIONAL CURRENCY

The functional and presentation currency of the Company is the Canadian dollar. The functional currency of TI Canada is the Canadian dollar and the functional currency of TI USA and TIWH is the US dollar.

3 SIGNIFICANT ACCOUNTING POLICIES, CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES

The accounting policies applied in the preparation of these consolidated financial statements are set out below:

3.1 REVENUE RECOGNITION

Effective January 1, 2018, Tree Island adopted the new reporting standard IFRS 15 Revenue from Contracts with Customers. IFRS 15 establishes a more structured approach to measuring and recognising revenue. The methodology to recognize revenue under IFRS 15 is aligned and consistent with the Company's existing method of recognizing revenues. Subsequently, the application of IFRS 15 did not result in significant changes to how the Company recognizes revenue and presents revenues in its financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

Tree Island recognizes revenue on the sale of goods when control passes to the buyer which is typically when the product is shipped. Revenue related to contract manufacturing (also known as tolling) is recognized at the point at which the items are ready to ship to the customer. For both the sale of goods and contract manufacturing, revenue is stated net of early payment discounts, freight where applicable, and rebates granted.

Early payment discounts are recognized on an invoice-by-invoice basis (not in aggregate) prior to the early payment date, and if the early payment date lapses without payment being made, the early discount amount forfeited will be recognized as revenue.

Volume rebates discounts are recognized separately for each customer by first estimating the rebate payable for the year based on the most likely amount method and allocating the expected rebates proportionately to each performance obligation.

3.2 CASH

Cash is comprised of bank balances, including outstanding items in deposit and net of outstanding disbursement accounts, cash balances in excess of revolving credit outstanding on the Senior Credit Facility (as defined in Note 8) and cash on hand.

3.3 INVENTORIES

Raw materials and consumable supplies and spare parts inventories are stated at the lower of weighted average cost and net realizable value. Finished and semi-finished products are stated at the lower of weighted average cost and net realizable value. Cost for finished and semi-finished products includes direct costs incurred in production including direct labour, materials, freight, depreciation and directly attributable overhead costs and indirect overhead costs based on normal operating capacity. Net realizable value is the estimated selling price in the ordinary course of business less estimated costs to sell. Consumable supplies and spare parts are inventories that are expected to be consumed in operations.

3.4 PROPERTY, PLANT AND EQUIPMENT AND DEPRECIATION

No depreciation is charged on capital projects during the period of construction. Costs are recognized net of government incentives. Regular repair and maintenance costs are recognized in the consolidated statement of operations as incurred. Depreciation is determined using the straight-line method over the estimated useful lives of the depreciable assets. When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment. Depreciation methods, asset residual values and useful lives are reviewed annually and adjusted prospectively as required.

Depreciation is calculated over the following rates:

Land	not depreciated
Buildings and improvements	19 to 30 years
Leasehold improvements	based on the term of the respective lease
Machinery and equipment	3 to 20 years

An item of property, plant and equipment and any significant part initially recognized is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated statement of operations when the asset is derecognized.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

3.5 IMPAIRMENT OF NON-FINANCIAL ASSETS

3.5.1 IMPAIRMENT CHARGES

Tree Island performs impairment tests on property, plant and equipment when events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss, if any, is determined as the excess of the carrying value of the asset over its recoverable amount, and is recognized in the consolidated statement of operations.

Tree Island assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists Tree Island estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's ("CGU") fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

In determining fair value less costs to sell, fair value is based on quoted market prices, prices for similar assets or other valuation techniques. The impairment analysis contains estimates due to the inherently speculative nature of forecasting long-term estimated cash flows and determining the ultimate useful lives of assets. If any of these estimates change, future net cash flows from the assets could be lower, which would result in additional impairment. As well, as much as practicable, third-party valuers are used to provide fair values which also contain assumptions concerning current market information for similar or same assets and if applicable functional and economic obsolescence.

Impairment losses of continuing operations are recognized in the consolidated statement of operations in those expense categories consistent with the function of the impaired asset.

3.6 FAIR VALUE MEASUREMENT

The Company measures financial instruments such as derivatives at fair value at each statement of financial position date. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 15.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible by the Company. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All financial assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorized within the fair value hierarchy (Note 15.2)

For assets and liabilities that are measured at fair value on a recurring basis, the Company determines whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

3.7 FINANCIAL INSTRUMENTS AND RISKS

Effective January 1, 2018, Tree Island adopted the new reporting standard IFRS 9 Financial Instruments, which replaces the previous standard IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 introduced new requirements for classifying and measuring financial instruments. Tree Island already recognizes and measures its financial instruments in a manner that is consistent with those required in IFRS 9. As such, the application of IFRS 9 did not result in significant changes to how financial instruments are currently measured and presented in the financial statements.

3.7.1 Financial Assets

Financial assets initially measured at fair value and thereafter at amortized cost include accounts receivables. The financial assets are classified depending on the business model for which the financial assets were acquired.

Financial assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are classified as current assets or non-current assets based on their maturity date.

Tree Island assesses at each reporting date whether there is objective evidence that financial assets are impaired. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in payments, the probability that they will enter bankruptcy or other financial reorganization. Impaired loans and receivables are charged to the consolidated statement of operations as bad debts and allowance for doubtful accounts is recognized. The allowance for doubtful accounts is determined using the expected credit loss model.

3.7.2 FINANCIAL LIABILITIES

Financial liabilities initially measured at fair value and thereafter at amortized cost include the Senior Credit Facility, accounts payable and other accrued liabilities, senior term loans, and long-term debt.

Financial liabilities are classified as current or non-current based on their maturity date and recognized initially at fair value, net of transaction costs incurred and are subsequently stated at amortized cost. Any difference between the amounts originally received, net of transaction costs, and the redemption value is recognized in the consolidated statement of operations over the period to maturity using the effective interest method.

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

3.7.3 FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT AND LOSS

Financial instruments at fair value through profit and loss are initially recognized at their fair value on the date the contract or transaction is entered into and are subsequently re-measured at their fair value at each reporting period with changes in the fair value recognized through the consolidated statement of operations. Financial instruments

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

at fair value through profit and loss include the change in purchase agreements for zinc (Note 15) and foreign exchange forward contracts (Note 15).

3.8 LEASES

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date and leases are classified as either finance or operating. Leases that transfer substantially all the benefits and risks of ownership of the leased item to Tree Island are accounted for as finance leases. Assets under finance lease are accounted for as assets and amortized over the lesser of the estimated useful life or the lease term. A finance lease obligation is recognized to reflect the present value of future lease payments and the finance element of the lease payments is charged to income over the term of the lease.

Operating lease payments are recognized as an operating expense in the consolidated statement of operations on a straight-line basis over the term of the lease.

3.9 PROVISIONS

3.9.1 GENERAL

Provisions are recognized when Tree Island has an obligation (legal or constructive) as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made on the amount of the obligation. Where Tree Island expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated statement of operations, net of any reimbursement.

3.9.2 ASSET DECOMMISSIONING AND RETIREMENT OBLIGATIONS

Tree Island recognizes obligations associated with the retirement of property, plant and equipment that result from the acquisition, construction, development or normal operations of the assets. These obligations, if material, are recorded at fair value and capitalized and depreciated as part of the cost of the related asset. Management has determined that Tree Island does not have any material asset decommissioning or retirement obligations.

3.10 POST-RETIREMENT BENEFITS

Tree Island contributes to a group registered retirement savings plan for Canadian employees and a 401K plan for US employees. The cost of these plans are expensed as earned by employees.

3.11 TAXES

3.11.1 CURRENT INCOME TAX

Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date in the countries where Tree Island operates and generates taxable income.

Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

3.11.2 DEFERRED TAX

Deferred tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date.

Deferred tax assets and liabilities are recognized for all taxable temporary differences, except in respect of taxable temporary differences associated with investments in subsidiaries when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary difference to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax losses can be utilized, except in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

3.11.3 SALES TAX

Revenues, expenses and assets are recognized net of the amount of sales tax, except when the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case, the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item, as applicable.

Receivables and payables are stated with the amount of sales tax included.

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the consolidated statement of financial position.

3.12 NET INCOME (LOSS) PER SHARE

Basic net income (loss) per Share is calculated by dividing net income (loss) by the weighted-average number of Shares outstanding during the period. Diluted net income (loss) per Share is calculated by factoring in the impact of dilutive instruments, if applicable.

3.13 FOREIGN EXCHANGE

Transactions in currencies other than the functional currency are recorded at the rate of exchange prevailing on the date of the transaction. Monetary assets and liabilities that are denominated in foreign currencies are translated at the rate prevailing at each reporting date. Non-monetary assets and liabilities denominated in foreign currencies

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

are retranslated to the functional currency at the exchange rate at the date of the transaction. Non-monetary items that are measured at historical cost in a foreign currency are translated at the exchange rate on the date of the transaction.

On consolidation the assets and liabilities of foreign operations are translated into Canadian dollars at the rate of exchange prevailing at the reporting date and their consolidated statement of operations are translated at exchange rates prevailing at the dates of the transactions. The exchange differences arising on translation for consolidation are recognized in other comprehensive income.

3.14 CRITICAL ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of consolidated financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingencies as at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant areas that involve estimates are listed below:

3.14.1 INVENTORY VALUATION

Inventories are recognized at the lower of cost or their Net Realizable Value (“NRV”), which is the estimated selling price in the ordinary course of business less the estimated costs of completion and estimated costs necessary to make the sale. IFRS requires that the estimated NRV be based on the most reliable evidence available at the time the estimates are made of the amounts that inventories are expected to realize.

The measurement of an inventory write-down to NRV is based on our best estimate of the NRV and of our expected future sale or consumption of our inventories. Due to market driven fluctuations in certain product group sales prices and the commodity nature of our significant raw materials, there is uncertainty as to whether the NRV of the inventories will remain consistent with those used in our assessment of NRV at period end. As a result there is the risk that a write-down of on-hand and unconsumed inventories could occur in future periods. Also, a certain portion of inventory may become damaged or obsolete. A slow moving reserve is recorded, as required, based on an analysis of the length of time product has been in inventory and historical rates of damage and obsolescence. Refer to Note 6 for the inventory provision as at December 31, 2018 and 2017.

3.14.2 ALLOWANCE FOR DOUBTFUL ACCOUNTS

It is possible that a certain portion of required customer payments will not be made, and as such an allowance for these doubtful accounts is maintained. The allowance is based on estimation of the potential of recovering the accounts receivable and incorporates current and expected collection trends. The estimates will change, as necessary, to reflect market or specific industry risks, as well as known or expected changes in the customers’ financial position. Refer to Note 5 for the carrying amount of allowance for doubtful accounts as at December 31, 2018 and 2017.

3.14.3 PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment comprises a large component of the total assets of Tree Island and as such the capitalization of costs, the determination of estimated recoverable amounts and the estimates of useful lives of these assets have a significant effect on Tree Island’s financial results.

During the repair and maintenance of an asset, the useful life of the respective asset may be reviewed and revised as appropriate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

The carrying value of plant, property and equipment is reviewed at the end of each reporting period. The impairment analysis contains estimates that can change due to the inherently speculative nature of forecasting long-term estimated cash flows and determining the ultimate useful lives of assets. If any of these estimates change significantly, future net cash flows from the property, plant and equipment could be lower or higher, which would result in additional impairment or reversal of impairments recognized in prior periods. As well, as much as practicable, third-party valuers are used to provide fair values that also contain assumptions concerning current market information for similar or same assets and if applicable functional and economic obsolescence.

3.14.4 INCOME TAXES

As at each consolidated statement of financial position date, a deferred income tax asset would be recognized for all deductible temporary differences, unused tax losses and income tax reductions, but only to the extent that their realization is probable. The determination of this requires significant judgment. This evaluation includes review of: (1) the ability to carry back operating losses to offset taxes paid in prior years; (2) the carry-forward periods of the losses; (3) an assessment of the excess of fair value over the tax basis of Tree Island's net assets, and, (4) appropriate and feasible corporate actions with respect to repatriation of foreign earnings. If, based on this review, it is not probable such assets will be realized, then no deferred income tax asset is recognized. Refer to Note 14.2 for deferred income tax assets and liabilities as at December 31, 2018 and 2017.

4 FUTURE IFRS STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE

Tree Island prepares its financial statements in accordance with IFRS standards. IASB has issued a new standard that will come into effect on January 1, 2019 that will have an impact on the Company's reporting requirements include:

IFRS 16 Leases

IFRS 16 was issued in January 2016 and provides guidance on how leases are to be recognized, measured, presented and disclosed. The standard provides a single lessee accounting model, requiring lessees to recognize leases as both assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. This standard is a significant change for how a lessee will recognize a lease from the standard it replaces, IAS 17. The accounting of leases by lessors under the new standard remains substantially unchanged from IAS 17. The standard is effective for annual periods beginning on or after January 1, 2019, with early application permitted for entities that apply IFRS 15.

The Company concluded a preliminary assessment of whether there will be any significant changes to its accounting policies and consolidated financial statements upon adoption of the new standard. The estimated impact of IFRS 16 on the Company's financial statements as at December 31, 2018 and for the year then ended is as follows:

- An approximate increase in fixed assets, via the recording of a right-of-use asset, of \$32 million;
- The recording of a lease liability in the amount of approximately \$34 million;
- An approximate decrease in equity in the amount of \$2 million;
- An approximate increase in gross profit for an amount of \$2 million due to a reduction in operating lease expenses;
- An approximate increase in depreciation expense from the right-of-use assets of \$2 million;
- An approximate increase in interest expense of \$1 million; and
- An approximate decrease in net income of \$1 million.

The Company will adopt the standard on its effective date using the modified retrospective approach and will apply practical expedient for low value and short-term leases. As IFRS 16 will result in a material impact on how leases are recognized and reported, we will continue to review the standard and any associated disclosure requirements to complete our comprehensive evaluation of the impacts of the standard on our consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

5 REVENUE AND ACCOUNTS RECEIVABLE

Revenue is inclusive of the cost of freight associated with those sales to customers where the Company arranges the freight. In 2018, this amounts to \$15.2 million (\$16.2 million in 2017).

Below is the composition and aging of Tree Island's accounts receivable:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Current	20,945	23,590
30 - 60 days past due	1,657	1,255
61 - 90 days past due	784	265
Over 91 days past due	1,066	1,375
Total accounts receivable	24,452	26,485
Allowance for doubtful accounts	(324)	(338)
Net accounts receivable	24,128	26,147

Accounts receivable are non-interest bearing and are generally due on 30-day to 90-day terms. The maximum credit risk that Tree Island was exposed to by way of its accounts receivable is equal to the net amount of \$24.1 million as at December 31, 2018 (\$26.1 million as at December 31, 2017).

At the end of each reporting period a review of the allowance for bad and doubtful accounts is performed. It is an assessment of the expected credit loss associated with trade accounts receivable after the consolidated statement of financial position date. The assessment is made by reference to age, status and risk of each receivable, current economic conditions and historical information. The trade accounts receivable balance is reduced through the use of the allowance for doubtful accounts and the amount of the loss is recognized in the consolidated statement of operations. Reversals to the allowance for doubtful accounts occur when previously allowed for trade accounts receivable are collected. Individual trade accounts receivable, together with any associated allowance previously recognized, are written off when there is no realistic prospect of future recovery. Accounts receivable with related parties are discussed in Note 12.1.

The following table represents a summary of the movement of the allowance for doubtful accounts:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Opening balance – January 1	338	259
Additions during the period	134	88
Reversals during the period	2	10
Collections	(19)	(12)
Write-offs during the period	(143)	-
Foreign exchange revaluation	12	(7)
Closing balance – December 31	324	338

See Note 15.3 on credit risk of trade receivables to understand how credit quality of accounts receivable that are neither past due nor impaired are managed and measured.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

6 INVENTORIES

Tree Island had the following categories of inventory:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Raw materials	27,599	16,529
Finished and semi-finished products	38,558	29,216
Consumable supplies and spare parts	15,462	14,247
Total inventory	<u>81,619</u>	<u>59,992</u>

At each year end, the ending inventories on hand are reviewed to determine if a write down to net realizable value is required. Based on this review, it was determined that no write-downs were necessary in 2018 and no write-downs were required in 2017. The reserves for slow moving inventory as at December 31, 2018 were \$1.4 million (\$1.4 million at December 31, 2017).

For the full year ended December 31, 2018 and 2017, Tree Island recognized, in income, inventory costs for the following:

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Opening inventory	59,992	67,268
Raw material purchases	161,591	130,745
Finished goods purchased for resale	7,842	7,717
Conversion costs	58,171	67,485
Closing inventory	<u>(81,619)</u>	<u>(59,992)</u>
Cost of sales	<u>205,977</u>	<u>213,223</u>

7 PROPERTY, PLANT AND EQUIPMENT

The carrying value of property, plant and equipment is reviewed each reporting period. For the purposes of testing for impairment, or the reversal of impairment, Tree Island Steel's assets are grouped and tested at the CGU level. Tree Island considers both qualitative and quantitative factors when determining whether an asset may be impaired, or when a reversal of impairment is required. Where the carrying value of the assets is not expected to be recoverable from future cash flows, they are written down to their recoverable amount. Tree Island has written down certain capital equipment related to the Residential product lines in the U.S. for \$0.7 million in 2018 and no write down in 2017.

From time to time we make investments to update, replace or make additions to our existing capital assets, which includes, but is not limited to, the buildings we occupy and capital equipment. These investments are in our normal course of business activity. For capital assets we have committed to purchase but have not yet received the amounts remaining to be paid are recognized as purchase commitments (refer to section 18.2).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

The net book value of the Company's property, plant and equipment is detailed below:

(\$'000 unless otherwise stated)

	Land & Improvement	Building & Improvement	Machinery & Equipment	Capital in Progress	Total
Cost					
As at December 31, 2016	9,835	43,432	29,550	1,076	83,893
Additions	-	1,464	1,804	2,813	6,081
Disposals	-	(7)	(298)	-	(305)
Foreign exchange translation	(140)	(563)	(496)	20	(1,179)
As at December 31, 2017	9,695	44,326	30,560	3,909	88,490
Additions	-	608	2,818	5,299	8,725
Disposals	-	(80)	(181)	-	(261)
Foreign exchange translation	174	806	651	141	1,772
As at December 31, 2018	9,869	45,660	33,848	9,349	98,726
Depreciation and impairment					
As at December 31, 2016	8	31,253	13,021	-	44,282
Depreciation for the period	16	1,262	2,252	-	3,530
Disposals	-	(7)	(227)	-	(234)
Foreign exchange translation	7	(277)	(508)	-	(778)
As at December 31, 2017	31	32,231	14,538	-	46,800
Depreciation for the period	16	1,271	2,206	-	3,493
Disposals	-	(80)	(134)	-	(214)
Foreign exchange translation	(6)	389	1,034	-	1,417
As at December 31, 2018	41	33,811	17,644	-	51,496
Net book value as at					
December 31, 2017	9,664	12,095	16,022	3,909	41,690
December 31, 2018	9,828	11,849	16,204	9,349	47,230

8 SENIOR CREDIT FACILITY

On July 1, 2018, the Company renewed its senior banking facility with Wells Fargo Capital Finance Corporation Canada ("Wells Fargo"). The five-year senior secured committed banking facility (the "Senior Credit Facility") which matures in June of 2023, may be used for Tree Island's financing requirements in Canadian and/or U.S. dollars, and comprises of the following:

- \$60 million of revolving credit facility;
- \$10 million "Fixed Asset Term Loan" applied against existing term loans; and
- \$10 million "Capex Term Loan" to finance future capital expenditures.

8.1 Senior Credit Facility

The amount advanced under the Senior Credit Facility at any time is limited to a defined percentage of inventories, accounts receivable, machinery and equipment, and real estate, less certain reserves. The Senior Credit Facility is secured by a first charge over Tree Island's assets supported by the appropriate guarantees, pledges and assignments, and requires that certain covenants be met by Tree Island.

The Senior Credit Facility includes a \$10.0 million Letter of Credit sub-facility which enables TI Canada and TI USA to open documentary and standby letters of credit for raw material purchases. There was a \$39 thousand Letter of Credit outstanding as at December 31, 2018.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

The amount available under the revolving portion of the Senior Credit Facility is limited to the amount of the calculated borrowing base, less issued Letters of Credit. The borrowing base is calculated as 90% of eligible receivables, plus the lesser of (a) 90% of the net orderly liquidation value of inventory and (b) 70% of eligible inventory.

Interest payable on funds borrowed in Canadian currency is at variable rates based on the Canadian Dollar Offered Rate ("CDOR") for Canadian dollar banker's acceptance. Interest payable on funds borrowed in U.S. currency is at variable rates based on the London Interbank Offered Rate ("LIBOR") for U.S. dollar deposits.

The following amounts are outstanding under the revolving portion of the Senior Credit Facility:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Revolving portion of the senior credit facility	49,797	33,468
Deferred financing costs	(182)	(69)
Total	<u>49,615</u>	<u>33,399</u>

The revolving portion of the Senior Credit Facility denominated in US dollars as at December 31, 2018 is \$19.4 million (\$22.6 million in 2017).

Deferred financing costs are included in other non-current assets on the consolidated statement of financial position.

The Senior Credit Facility has financial tests and other covenants with which the Company and its subsidiaries must comply, the primary one being based on the remaining funds within the senior credit facility that is available ("Availability Test"). Only if the Availability Test falls below a certain threshold then other covenants, which include a rolling four quarters defined fixed charge coverage ratio of 1:1, are tested. As well, the Senior Credit Facility contains restrictive covenants that limit the discretion of the Company's management with respect to certain business matters. These covenants place restrictions on, among other things, the ability of the Company's operating subsidiaries to incur additional indebtedness, to create liens or other encumbrances, to pay dividends or make certain other payments, investments, loans and guarantees and to sell or otherwise dispose of assets and merge or consolidate with another entity.

As at December 31, 2018, the availability was in excess of the Availability Test and the Company was in compliance with its financial covenants on the Senior Credit Facility.

8.2 Senior Term Loans

Under the terms of the Senior Credit Facility, the Company has designated portions up to a total of \$20 million as two term loans denominated in either Canadian or U.S. dollars, and is available for existing machinery and equipment and future capital expenditures. The existing term debts applied against the Senior Credit Facility was incorporated into a single term loan of \$10 million, denominated in Canadian dollars on July 1, 2018, referred to as "Fixed Asset Term Loan". An additional \$10 million is available to finance future capital expenditures, to be denominated in either Canadian or U.S. dollars and referred to as "Capex Term Loans". On September 24, 2018, \$3.8 million was applied against the Capex Term Loan of the Senior Credit Facility for financing a new concrete mesh machine in our U.S. Operations.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

The following amounts are outstanding under the Senior Term Loans:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Senior term loans - beginning of period	10,546	12,369
Advances	3,758	-
Foreign exchange revaluation	202	(74)
Payments	(1,171)	(1,749)
Senior term loans - end of period	13,335	10,546
Less: current portion	(1,986)	(1,738)
Total	<u>11,349</u>	<u>8,808</u>

9 LONG-TERM DEBT

In June of 2012, the Company entered into long-term debt agreements with a trade creditor. The repayment schedule of the long-term debt extends to June 2028 with principal payments over a 10 year amortization period. The interest is non-compounding interest at 4% and commenced accruing June 2017 and will become payable monthly over 4 years commencing June 2024. Principal payments, which started in 2009, are monthly in the amounts of US\$100k in years 1 and 2, US\$110k in years 3 and 4, US\$120k years 5, 6 and 7, and US\$190k in years 8, 9,10 and \$90k in years 11, 12 and 13. Present value of the debt was determined using discounted cash flows and a credit adjusted discount rate of 9%. The discount rate, together with the stated interest, comprises the debt discount. Using the effective interest rate method, the debt discount is amortized as accretion and charged to interest expense over the term of the amended long-term debt agreements.

The amounts owing under the long-term debts are denominated in U.S. dollars.

The elements of the long-term debt are listed below:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Beginning of period	8,187	10,256
Payments	(1,873)	(2,542)
Foreign exchange revaluation	671	(601)
Accretion of debt discount	931	1,074
End of period	7,916	8,187
Less: current portion	(2,994)	(1,806)
Net long-term debt	<u>4,922</u>	<u>6,381</u>

In addition, under the terms of this long-term debt agreement, Tree Island is required to make an accelerated payment of between \$0.3 million to \$0.5 million on the principal outstanding within 120 days of any fiscal year end in which EBITDA exceeds a specified amount.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

10 FINANCING EXPENSES

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Non-cash accretion of debt discount and interest on long term debt	931	1,074
Interest on senior credit facility (Note 8.1)	1,533	1,056
Other interest and financing costs	946	789
Amortization of deferred financing costs	90	48
Total	3,500	2,967

11 SHAREHOLDERS' CAPITAL

Tree Island is authorized to issue an unlimited number of Shares. The Shares have no par value. There were no Shares issued and 466,149 Shares were repurchased (totaling \$1.3 million at an average price of \$2.71 per Share) and cancelled in the year ended December 31, 2018. Shares issued and outstanding are as follows:

(\$'000 except for Shares)

	Shares	Gross	Issuance Cost ²	Net
Shareholders' capital - December 31, 2016	31,064,573	241,823	11,400	230,423
Repurchase of common shares	(1,414,774)	(4,446)	-	(4,446)
Shareholders' capital - December 31, 2017	29,649,799	237,377	11,400	225,977
Repurchase of common shares	(466,149)	(1,262)	-	(1,262)
Shareholders' capital - December 31, 2018	29,183,650	236,115	11,400	224,715

11.1 NORMAL COURSE ISSUER BID

The Company has an ongoing normal course issuer bid (the "Bid"). The previous Bid was effective from September 21, 2017 to September 20, 2018 to purchase up to 1,500,000 Shares. The Company renewed the Bid, effective September 21, 2018 and expiring September 20, 2019. The renewed Bid allows the Company to purchase up to 1,460,000 Shares in the period. Tree Island has no obligation to purchase any Shares under the Bid.

For the period January 1, 2018 to September 20, 2018 the Company purchased 362,169 Shares under the previous Bid at a total cost of \$1.0 million (at an average price of \$2.77 per Share). Under the current Bid from September 21, 2018, the Company purchased 103,980 at a total cost of \$0.3 million (at an average price of \$2.49 per Share). All 466,149 Shares purchased were cancelled prior to December 31, 2018.

12,695 Shares were purchased under the Bid for the period January 1, 2019 to February 20, 2019.

² Issuance costs were incurred as a result of the November 2002 Initial Public Offering and October 2004 Secondary Offering.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

12 RELATED PARTY TRANSACTIONS

12.1 TRANSACTIONS WITH ASSOCIATED COMPANIES

The Futura Corporation (“Futura”) is considered to be a related party to the Company because of its share ownership interest and the fact that Mr. Doman, the sole shareholder and president of Futura, and Mr. Rosenfeld, the Executive Vice President of Futura, sit on the Board of Directors.

Based on Tree Island Steel’s outstanding Shares as at February 20, 2019, Futura owns 30.2% of the fully diluted Shares of the Company.

In addition, Mr. Doman is Chairman and CEO of CanWel Building Materials Group Ltd. (“CanWel”). For the year ended December 31, 2018, Tree Island sold, net of rebates, approximately \$3.6 million (\$2.9 million in 2017) of goods to CanWel and trade accounts receivable owing from CanWel as at December 31, 2018 is approximately \$0.1 million (approximately \$0.1 million in 2017). Outstanding trade accounts receivable from CanWel at period end are unsecured, interest free and settlement occurs in cash (Note 5).

12.2 TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL

Included in the definition of key management for purposes of disclosure of related party transactions are members of Board of Directors and officers of Tree Island Steel. Amounts for key management personnel for the year ended December 31, 2018 was approximately \$2.9 million (approximately and \$2.7 million in 2017) which includes wages, salaries and social security contributions, paid annual and sick leave, vehicle costs, bonuses and severance amount payable to an officer. It also includes directors’ fees paid to members of the Board.

13 POST RETIREMENT BENEFITS

Tree Island contributes to a group registered retirements savings plan for all eligible Canadian employees and a 401K for all eligible US employees. Contributions made by Tree Island’s subsidiaries in 2018 amounted to \$1.4 million (\$1.5 million in 2017). Funding obligations are satisfied upon making contributions.

14 INCOME TAXES

14.1 INCOME TAX RECOVERY (EXPENSE)

The income tax recovery (expense) is divided between current and deferred taxes as follows:

(\$’000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Current tax recovery (expense)	(332)	(2)
Deferred tax recovery (expense)	(1,838)	(1,781)
Total in the Consolidated Statement of Operations	<u>(2,170)</u>	<u>(1,783)</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

The expense or recovery of income taxes varies from the amount that would be expected if computed by applying the Canadian federal and provincial and US federal and state statutory income tax rates to the income before income taxes as shown in the following table:

(\$'000 unless otherwise stated)

	As at December 31,	
	2018	2017
Income (loss) before provision for income taxes	4,763	145
Tax Rate	27.0%	26.0%
Expected income tax recovery (expense)	(1,286)	(38)
Revisions to prior year estimates	(582)	(70)
Items not deductible for tax	(65)	(100)
Foreign exchange on intercompany loans	(681)	556
Differential tax rates on U.S. subsidiary	-	784
Change in unrecognized deferred tax benefits	538	(2,920)
Loss previously not recognized	-	75
Other	(94)	(70)
Total in the Consolidated Statement of Operations	(2,170)	(1,783)

14.2 DEFERRED INCOME TAX ASSETS AND LIABILITIES

The components of deferred income tax assets and liabilities as at December 31 are as follows:

(\$'000 unless otherwise stated)

	As at December 31,	
	2018	2017
Non-capital tax loss-carry forwards	1,340	3,449
Property, plant and equipment	(4,729)	(4,774)
Long-Term Debt	380	106
Unrealized foreign exchange (gain) loss	-	(18)
Reserves and other liabilities	-	(20)
Interest and other	(222)	(161)
Deferred tax asset (liability)	(3,231)	(1,418)
Deferred tax (liability) beginning of year	(1,418)	417
Deferred tax recovery (expense) during the year	(1,838)	(1,781)
Deferred tax asset (liability) - Other	25	(54)
Deferred tax asset (liability) end of year	(3,231)	(1,418)

No deferred tax assets have been recognized on the consolidated statements of financial position where Tree Island has concluded that it is not probable that the benefits of recognized deferred income tax assets will be realized prior to their expiry. As such, Tree Island has not recognized a deferred tax asset on the following items:

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(\$'000 unless otherwise stated)

	As at December 31,	
	<u>2018</u>	<u>2017</u>
Non-capital tax loss carry-forwards	68	-
Goodwill and intangibles	168	198
Unrealized foreign exchange losses	804	829
Reserves and other liabilities	313	232
Capital losses	2,715	1,882
Interest and other	7,832	6,566
Deferred tax asset	<u>11,900</u>	<u>9,707</u>

14.3 INCOME TAX LOSS CARRY-FORWARDS

As at December 31, 2018, Tree Island had income tax loss carry forwards available to offset future taxable income with expiries as shown in the table below:

(\$'000 unless otherwise stated)

<u>Year of Expiration</u>	<u>Canada</u>	<u>US - Federal</u>	<u>US - State</u>
2031	27	-	7,447
2032	265	-	503
2033	-	-	1,345
2034	-	-	3,717
2035	-	-	2,316
2036	-	3,966	4,597
Total	<u>292</u>	<u>3,966</u>	<u>19,927</u>

As at December 31, 2018, the Company had capital losses of \$20.5 million in addition to the non-capital loss carry forwards listed above. The capital losses can be carried forward indefinitely to offset against future capital gains in Canada.

15 FINANCIAL INSTRUMENTS

15.1 FAIR VALUE OF FINANCIAL INSTRUMENTS

Tree Island records certain of its financial instruments at fair value using various techniques. These include estimates of fair values based on prevailing market rates (bid and ask prices, as appropriate) for instruments with similar characteristics and risk profiles or internal or external valuation models, such as discounted cash flow analysis and option pricing models, using, to the extent possible, observable market-based inputs.

The fair values of the financial assets and financial liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than a forced or liquidation sale. The following methods and assumptions were used to estimate the fair values:

- Cash, accounts receivable, the revolving portion of the Senior Credit Facility and accounts payable and accrued liabilities approximate their carrying amounts largely due to the short-term nature of these instruments and interest rates being variable for the senior credit facility;
- Fair value on the Company's Senior Term Loans and Long-Term Debt are based on estimated market interest rate on similar borrowings. The carrying value of the Senior Term Loans approximates fair value as the

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

interest rates approximate market. A 1% change in the market interest rate would change the fair value of Long-Term Debt by \$0.2 million and Senior Term Loans by \$0.1 million;

- Fair value of the commodity purchase contract embedded derivatives are estimated using observable spot rates for zinc; and
- Fair value of the forward exchange forward contracts is estimated using observable foreign exchange spot and forward rates. The Company does not consider interest rates or the credit quality of counterparties as significant inputs to the valuation.

(\$'000 unless otherwise stated)

	As at December 31, 2018		As at December 31, 2017	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Cash and cash investments	1,277	1,277	1,651	1,651
Accounts receivable	24,128	24,128	26,147	26,147
Total financial assets	<u>25,405</u>	<u>25,405</u>	<u>27,798</u>	<u>27,798</u>
Senior revolving facility	49,797	49,797	33,468	33,468
Accounts payable and accrued liabilities	22,017	22,017	18,272	18,272
Senior term loans	13,335	13,335	10,546	10,546
Long-term debt	7,916	7,041	8,187	7,920
Commodity purchase derivative	-	-	67	67
Total financial liabilities	<u>93,065</u>	<u>92,190</u>	<u>70,540</u>	<u>70,273</u>

15.2 FAIR VALUE HIERARCHY

The financial instruments have been categorized on a fair value hierarchy based on whether the inputs to those valuation techniques are observable (inputs reflect market data obtained from independent sources) or unobservable (inputs reflect the Company's market assumptions).

The three levels of fair value estimation are:

Level 1: Quoted (unadjusted) market prices in active markets for identical assets or liabilities;

Level 2: Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable; and

Level 3: Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

The only financial estimates carried at fair value are commodity purchase derivatives, which are level 2 financial instruments.

15.3 RISK EXPOSURE AND MANAGEMENT

Tree Island is exposed to various risks associated with its financial instruments. These risks are categorized as credit risk, liquidity risk and market risk.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

15.3.1 CREDIT RISK

Credit risk consists of credit losses arising in the event of non-payment of accounts receivable of customer accounts. However, the credit risk is minimized through selling to well-established customers of high-credit quality. The credit worthiness of customers is assessed using credit scores supplied by a third party and through direct monitoring of their financial well-being on a continual basis. Management establishes guidelines for customer credit limits and should thresholds in these areas be reached, appropriate precautions are taken to manage credit risk. Provisions for potential credit losses (allowance for doubtful accounts) are maintained and any such losses to date have been within management's expectations.

15.3.2 LIQUIDITY RISK

Liquidity arises from our financial obligations and in the management of our assets, liabilities and capital structure. This risk is managed by regular evaluation of our liquid financial resources to fund current and long-term obligations and to meet its capital commitments in a cost-effective manner.

The main factors that affect liquidity include realized sales prices, production levels, cash production costs, working capital requirements, future capital expenditure requirements, scheduled payments on financial liabilities and lease obligations, credit capacity and expected future debt and equity capital market conditions.

Liquidity requirements are met through a variety of sources including cash balances on hand, cash generated from operations, existing credit facilities, and debt and equity capital markets. Management monitors and manages liquidity risk by preparing annual budgets, monthly projections to the end of the fiscal year and regular monitoring of financial liabilities against the constraints of the available revolving credit facilities.

The table below summarizes the future undiscounted contractual cash flow requirements for financial liabilities (including scheduled interest payments on interest bearing liabilities) as at December 31, 2018:

(\$'000 unless otherwise stated)

	Carrying Amount	Contractual Cash Flow	Less Than 1 Year	1 – 2 Years	Greater Than 2 Years
Senior revolving facility	49,797	49,797	49,797	-	-
Accounts payable and accrued liabilities	22,017	22,017	22,017	-	-
Senior term loans	13,335	13,335	1,986	3,972	7,377
Long-term debt	7,916	11,616	2,994	3,028	5,594
As at December 31, 2018	93,065	96,765	76,794	7,000	12,971

15.3.3 FOREIGN CURRENCY RISK

Tree Island's U.S. dollar-denominated cash, accounts receivable, accounts payable and accrued liabilities, Senior Credit Facility and Long-Term Debt are exposed to foreign currency exchange rate risk because the value of these financial instruments will fluctuate with changes in the U.S./Canadian dollar exchange rate. The Company enters into U.S. dollar currency forward contracts for periods consistent with a portion of U.S. dollar currency transaction exposures, generally from one to three months. These are not designated as cash flow, fair value or net investment hedges. As of December 31, 2018, the Company had no outstanding U.S. dollar currency forward contracts.

For the period ending December 31, 2018, a \$0.01 increase (decrease) in the Canadian dollar to U.S. dollar exchange rate will increase (decrease) net comprehensive income by \$6 thousand.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

15.3.4 INTEREST RATE RISK

Tree Island is exposed to interest rate risk on its Senior Credit Facility. Interest payable on the funds advanced under the Senior Credit Facility are based on the Canadian interbank bid rates for Canadian dollar banker's acceptance for Canadian dollar denominated borrowings or the London Inter-Market Offered Rate ("LIBOR") for U.S. dollar deposits for U.S. dollar denominated borrowings.

A one percent increase in the interest rates charged on the Senior Credit Facility would increase financing expenses by \$0.5 million annually. Tree Island does not use derivative instruments to manage the interest rate risk.

15.3.5 RAW MATERIAL PRICE RISK

Tree Island is exposed to changes in the price of the materials used in its production process and, from time to time, enters into forward contracts to purchase a portion of the zinc used. These are not designated as cash flow or fair value hedges. As at December 31, 2018, the Company had no outstanding zinc forward contracts.

16 MANAGEMENT OF CAPITAL

The Company's objectives when managing its capital are:

- To maintain a capital base so as to preserve and enhance investor, creditor, and market confidence and to sustain viability and future development of the business; and
- To manage capital in a manner that will comply with the financial covenants on the Senior Credit Facility, Senior Term Loan agreements and Long-Term Debt agreements as described further in Notes 8.1, 8.2 and 9.

Management manages the capital structure in accordance with these objectives, with considerations given to changes in economic conditions and the risk characteristics of the underlying assets in particular, by closely monitoring cash flows and compliance with external debt covenants. The table below is what management considers capital:

(\$'000 unless otherwise stated)

	As at December 31, 2018	As at December 31, 2017
Total shareholders' equity	58,626	59,269
Senior revolving facility	49,797	33,468
Senior term loans	13,335	10,546
Long-term debt	7,916	8,187
Total capital	<u>129,674</u>	<u>111,470</u>

17 NET INCOME PER SHARE

Basic earnings per Share amount is calculated by dividing net income for the year by the weighted average number of Shares outstanding during the year.

Diluted earnings per Share amount is calculated by dividing the net income for the year by the weighted average number of Shares outstanding during the year plus the weighted average number of Shares that would be issued on conversion of all the dilutive potential units into Shares. As at December 31, 2018 the Company does not have any instruments issued that could be dilutive.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

466,149 Shares were repurchased and cancelled for the year ended December 31, 2018 and 12,695 Shares were repurchased and cancelled from January 1, 2019 up to February 20, 2019 (Note 11).

The following reflects the income and Share data used in the earnings per Share computations:

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	<u>2018</u>	<u>2017</u>
Net income (loss) for the year	2,593	(1,638)
Weighted average number of shares outstanding:	29,411,890	30,623,785
Net income per share (\$/share)	0.09	(0.05)

18 PROVISIONS AND COMMITMENTS

18.1 LITIGATION AND CLAIMS

Tree Island is party to certain legal actions and claims, none of which individually, or in the aggregate, is expected to have a material adverse effect on its financial position, consolidated statement of operations or cash flows.

18.2 PURCHASE COMMITMENTS

As at December 31, 2018, Tree Island's wholly owned subsidiaries have committed to raw material purchases (including finished goods) totalling \$28.4 million (\$44.6 million in 2017). As at December 31, 2018, the Company also committed to payments on capital equipment, with the total amount outstanding totalling \$0.5 million (\$3.5 million in 2017).

18.3 OPERATING LEASE COMMITMENTS

Tree Island and its subsidiaries have various operating lease agreements with remaining terms of up to five years with varying renewal options. Annual lease rental payments due under non-cancelable operating leases are as follows:

(\$'000 unless otherwise stated)

	<u>As at December 31, 2018</u>
Less than 1 year	3,346
1 to 5 years	11,541
More than 5 years	16,282
Total capital	<u>31,169</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

19 SEGMENTED INFORMATION

19.1 MARKET SEGMENTS

Revenues for each group for the twelve months ended December 31, 2018 and 2017 were as follows:

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
Industrial	79,295	84,379
Commercial	54,375	44,753
Agricultural	28,044	28,886
Residential	73,592	76,687
Total revenue	<u>235,306</u>	<u>234,705</u>

Tree Island operates primarily within one industry, the steel wire products industry, with no separately reportable operating segments. Tree Island groups its products into the following: Industrial, Agricultural, Commercial Construction, and Residential Construction. No one customer is more than 10% of total revenue.

19.2 GEOGRAPHIC SEGMENTS

The products are sold primarily to customers in the United States and Canada and are attributed to geographic areas based on the location of customers:

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
United States	148,410	148,336
Canada	80,381	78,269
International	6,515	8,100
Total revenue	<u>235,306</u>	<u>234,705</u>

Non-current assets for this purpose consist of property, plant and equipment and other non-current assets. These assets are attributed to geographic areas based on the locations of the subsidiary company owning the assets.

(\$'000 unless otherwise stated)

	Years Ended December 31,	
	2018	2017
United States	17,110	12,315
Canada	30,302	29,444
Total non-current assets	<u>47,412</u>	<u>41,759</u>

SHAREHOLDER INFORMATION

TREE ISLAND STEEL

Board of Directors:

Amar S. Doman –
Chairman of the Board

Dale R. MacLean

Peter Bull

Harry Rosenfeld

Michael Fitch

Sam Fleiser

Theodore A. Leja

Joe Downes

Executive Officers:

Dale R. MacLean
*President and Chief
Executive Officer*

Remy Stachowiak
Chief Operating Officer

Nancy Davies
*Chief Financial Officer and
Vice President, Finance*

Shares:

Market Information

Tree Island Steel is listed on
the Toronto Stock Exchange
trading symbol: TSL.

Registrar and Transfer Agent

Computershare Investor
Services Inc.

Corporate Head Office:

3933 Boundary Road
Richmond, B.C.
Canada, V6V 1T8

Website:

www.treeisland.com

Investor Relations:

Ali Mahdavi
Investor Relations
(416)-962-3300 or
amahdavi@treeisland.com

Auditors:

KPMG LLP
Vancouver, B.C.

