Fortress Paper LTD.
TSX: FTP

Q3 2009

For the three months ended September 30, 2009

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FORTRESS PAPER LTD.
MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") of the financial condition and results of operations of Fortress Paper Ltd ("Fortress" or the "Company") has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and should be read in conjunction with the unaudited consolidated financial statements and the notes thereto for the three and nine month periods ended September 30, 2009 and with the audited consolidated financial statements for the year ended December 31, 2008 (available on SEDAR at www.sedar.com). The MD&A provides a review of the significant developments that have impacted the Company's performance during the quarter ended September 30, 2009 relative to the previous quarter and prior year comparative quarter.

This MD&A contains certain forward-looking statements that reflect the current views and/or expectations of the Company with respect to its performance, business and future events. The reader is cautioned that forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements including, without limitation, those relating to damage to our reputation, competition, maintaining our market position, marketability and price of our products, technology and protection of our intellectual property, dependence on our major customers, fluctuations in the price and supply of raw materials, fluctuations in foreign exchange and other risk factors detailed in our filings with Canadian securities regulatory authorities. These risks, as well as others, could cause actual results and events to vary significantly. The Company does not undertake any obligation to release publicly any revisions for updating any voluntary forward-looking statements, except as required by law.

Throughout this discussion, reference is made to EBITDA (defined as net income before interest, income taxes, depreciation, amortization, non-operating income and expenses and stock based compensation), which the Company considers to be an indicative measure of operating performance and a good metric to evaluate profitability. EBITDA is not a generally accepted earnings measure and should not be considered as an alternative to net income or cash flows as determined in accordance with GAAP. As there is no standardized method of calculating EBITDA, the Company's use of the term may not be directly comparable with similarly titled measures used by other companies. A reconciliation of EBITDA to net income reported in accordance with GAAP is included in this MD&A.

The information in this report is as at November 6, 2009.

All financial references are in Canadian dollars unless otherwise noted.

Highlights

Fortress Paper Ltd. reported net income of $3.5 million for the third quarter of 2009 on sales of $51.0 million or basic and diluted earnings per share of $0.34. For the third quarter of 2008 the Company reported net income of $2.3 million on sales of $43.7 million or basic and diluted earnings per share of $0.22. In the second quarter of 2009 the Company reported net income of $1.9 million on sales of $49.6 million or basic and diluted earnings per share of $0.19.

Adjusted net income for the third quarter of 2009 was $0.38 per share. Adjusted net income for the previous year comparative period and prior quarter was $0.34 per share and $0.27 per share.

EBITDA was $7.0 million or 13.7% of sales for the three months ended September 30, 2009. For the three months ended September 30, 2008 EBITDA was $6.2 million or 14.2% of sales. EBITDA for the second quarter of 2009 was $5.7 million or 11.5% of sales.

The increase in EBITDA relative to the prior year comparative period was primarily due to higher margin security paper sales at the Landqart mill and continued strong performance at the Dresden mill. The market for security papers, which includes bank notes, passport paper and other high security papers, continues to show strength and our order book for wallpaper base is experiencing its highest level of demand since the economic downturn.

Description of Business

The Company was incorporated on May 30, 2006 under the laws of the Province of British Columbia. Fortress Paper Ltd. is an international producer of security and other specialty papers. The Company owns and operates two paper mills, the Landqart mill located in Switzerland and the Dresden mill located in Germany. Fortress' security papers include banknote, passport and visa papers. The security papers produced at the Landqart mill incorporate internationally recognized overt and covert security features which are embedded into the paper and supplemented with customer-specific features. The Landqart mill has leveraged its extensive security papers competence to develop additional commercial applications using its in-house know-how and technology of security features to create innovative paper-based security products. Fortress' specialty papers business includes non-woven wallpaper base products, as well as graphic and technical papers. The Dresden mill produces coated and uncoated wallpaper base for wallpaper manufacturers.

Third Quarter 2009 Earnings Review

Three Months Ended September 30

Selected Financial Information and Statistics

(thousands of dollars, except shipments, unaudited)	Q3 2009	Q2 2009	Q3 2008
Sales	51,000	49,638	43,744
EBITDA[1]	6,967	5,699	6,234
Operating income	5,198	4,460	4,993
Net income	3,467	1,926	2,312
Shipments (tonnes)	14,304	14,181	12,843

[1]See net income to EBITDA reconciliation.

Analysis of Specific Items Affecting Comparability of Net Income

(thousands of dollars, except per share figures, unaudited)	Q3 2009	Q2 2009	Q3 2008
Net income as reported	3,467	1,926	2,312
Foreign exchange loss (gain)	365	766	1,257
Adjusted net income	3,832	2,692	3,569
Net income per share (EPS), as reported	0.34	0.19	0.22
Impact of above item per share	0.04	0.07	0.12
Adjusted net income per share	0.38	0.26	0.34

Overview

At the Landqart mill the market for security papers continues to show strength. The Landqart mill results for the quarter reflect higher margin banknote sales than in prior quarters.

At the Dresden mill, the wallpaper base market experienced strong orders throughout the third quarter. The Dresden mill has successfully completed the second stage of capital improvements to enhance the quality and efficiency of its production of non-woven wallpaper base. Despite the global crisis, profitability remains strong and the order book has improved to the highest levels of the year.

Sales. Sales for the three months ended September 30, 2009 were slightly higher relative to the second quarter of 2009 primarily due to the higher margin sales mix at Landqart offset by lower sales at the Dresden mill. Sales for the three months ended September 30, 2009 were higher when compared to the prior year comparative quarter due to the increased tonnes sold.

Cost of Products Sold. Cost of products sold were $38.4 million or 75.2% of sales for the three months ended September 30, 2009 compared to $31.6 million or 72.2% in the prior year comparative period. In the second quarter of 2009, cost of products sold were $38.6 million or 77.8% of sales.

Selling, General and Administrative. Selling, general and administrative expenses were $5.7 million (third quarter 2008, $5.9 million and second quarter 2009, $5.3 million) and were comprised primarily of sales commissions, marketing, corporate and administrative expenses.

Stock-based Compensation. Stock-based compensation expense was $0.4 million during the period (prior year comparative period, $0.4 million) and reflected 26,000 deferred share unit awards to non-employee directors and 147,100 restricted share unit awards to key employees.

EBITDA. As a result of the foregoing factors, EBITDA was $7.0 million in the third quarter of 2009 compared to $6.2 million in the third quarter of 2008 and $5.7 million in the second quarter of 2009.

Net income to EBITDA reconciliation:

(thousands of dollars, unaudited)	**Q3 2009**	**Q2 2009**	**Q3 2008**
Net income	$3,467	$1,926	$2,312
Income tax	1,090	1,511	1,382
Foreign exchange (gain) loss	365	766	1,257
Interest expense	276	257	42
Amortization	1,350	1,029	865
Stock based compensation	419	210	376
EBITDA	$6,967	$5,699	$6,234

Operating Results by Business Segment

Landqart Mill

(thousands of dollars, except for shipments, unaudited)	**Q3 2009**	**Q2 2009**	**Q3 2008**
Sales	23,989	20,861	19,080
Operating income	1,844	28	1,195
Shipments (tonnes)	4,145	4,127	4,286

Dresden Mill

(thousands of dollars, except for shipments, unaudited)	**Q3 2009**	**Q2 2009**	**Q3 2008**
Sales	27,011	28,777	24,664
Operating income	4,661	5,477	4,874
Shipments (tonnes)	10,159	10,054	8,557

Nine Months Ended September 30

Selected Financial Information and Statistics for the Nine Months Ended:

(thousands of dollars, except for shipments, unaudited)	September 30, 2009	September 30, 2008	September 30, 2007
Sales	147,261	142,671	107,757
EBITDA[1]	17,698	19,061	9,356
Operating income	13,423	15,595	7,218
Net income	8,977	9,902	3,005
Shipments (tonnes)	41,208	41,972	38,846

[1]See net income to EBITDA reconciliation.

Analysis of Specific Items Affecting Comparability of Net Income

(thousands of dollars, except per share figures, unaudited)	September 30, 2009	September 30, 2008	September 30, 2007
Net income as reported	8,977	9,902	3,005
Foreign exchange loss (gain)	76	484	380
Adjusted net income	9,053	10,386	3,385
Net income per share (EPS), as reported	0.88	0.97	0.52
Impact of above item per share	0.00	0.04	0.06
Adjusted net income per share	0.88	1.01	0.58

Overview

At the Landqart mill the market for security papers continues to show strength; however, specialty papers continued to experience challenges through the nine month period ended September 30, 2009 as a direct result of the global economic slowdown. When compared to the prior year period, current year to date results reflect weakness in the specialty papers which has been partially offset by strength in the security segment.

At the Dresden mill, the wallpaper base market experienced strengthening orders throughout the first nine months. Although sales tonnage has increased relative to the prior year, profitability is slightly lower at the Dresden mill due to product mix diversification. However, improved efficiencies on the paper machine at the Dresden mill has provided us with strong margins despite the economic slowdown.

Sales. Sales for the nine months ended September 30, 2009 were slightly higher relative to prior year comparative period primarily due to due to the product mix at the Landqart mill and continued strength at the Dresden mill.

Cost of Products Sold. Cost of products sold were $113.0 million or 76.8% of sales for the nine months ended September 30, 2009. In the nine months ended September 30, 2008 cost of products sold were $106.9 million or 74.9% of sales. Security and wallpaper base operated at full capacity during the period.

Selling, General and Administrative. Selling, general and administrative expenses were $16.5 million for the nine months ended September 30, 2009 and $16.7 million in the prior year comparative period.

Stock-based Compensation. Stock-based compensation expense was $0.8 million during the period (prior year comparative period, $1.1 million).

EBITDA. As a result of the foregoing factors, EBITDA was $17.7 million for the nine months ended September 30, 2009 compared to $19.1 for the nine months ended September 30, 2008.

Net income to EBITDA reconciliation:
(thousands of dollars, unaudited)

	September 30, 2009	**September 30, 2008**	**September 30, 2007**
Net income	8,977	9,902	3,005
Income tax	3,645	4,029	2,679
Other (income) expense	76	484	378
Interest expense	725	1,180	1,156
Amortization	3,446	2,338	1,517
Stock based compensation	829	1,128	621
EBITDA	17,698	19,061	9,356

Operating Results by Business Segment

Landqart Mill

(thousands of dollars, except for shipments, unaudited)	**September 30, 2009**	**September 30, 2008**	**September 30, 2007**
Sales	65,211	59,804	46,209
Operating income	2,712	2,767	1,854
Shipments (tonnes)	11,993	13,362	12,130

Dresden Mill

(thousands of dollars, except for shipments, unaudited)	**September 30, 2009**	**September 30, 2008**	**September 30, 2007**
Sales	82,050	82,867	61,548
Operating income	14,172	15,851	7,058
Shipments (tonnes)	29,215	28,610	26,716

Liquidity and Capital Resources

The Company's objectives when managing capital are to safeguard its assets and maintain a globally competitive cost structure while looking for growth opportunities to provide returns to its shareholders. In addition, the Company works with all relevant stakeholders to ensure the safety of its operations and employees, and remain in compliance with all environmental regulations and enhance the communities in which it operates.

The Company constantly monitors and assesses its financial performance in order to ensure that its net debt levels are prudent, taking into account the anticipated direction of the Company and business cycle. The company continuously monitors the public and private debt markets and the public equity markets in order to assure that its capital structure is appropriately balanced. The Company's results can be materially influenced by changes in the relative value of the Swiss Franc and Euro to the Canadian dollar.

Although there can be no assurances, Fortress believes that cash generated from operations, together with amounts available under its credit facilities and net proceeds from the IPO will be sufficient to meet its debt service requirements, capital expenditure needs and working capital needs for the foreseeable future. Fortress' future operating performance and its ability to service its debt will be subject to future economic conditions and the financial success of Fortress' business and other factors, many of which are not within Fortress' control, including changes in market prices for its security and specialty papers and raw material costs.

The Company's capital is comprised of net debt and shareholders' equity:

(thousands of dollars, except for shipments, unaudited)	**September 30, 2009**	**December 31, 2008**
Cash and cash equivalents	$ 28,368	$ 26,187
Less total debt	(31,183)	(30,591)
Net debt	$ (2,815)	$ (4,404)
Shareholders' equity	$ 82,712	$ 72,906

The Company is not subject to any externally imposed capital requirements.

Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Financial instruments that potentially subject the Company to credit risk include cash and cash equivalents and accounts receivable.

Cash and cash equivalents includes cash on deposit with an original maturity date of 90 days or less. In order to mitigate the risk of financial loss, cash on deposit is held with major Canadian and international financial institutions. The cash and cash equivalents balance at September 30, 2009 was $28.4 million (December 31, 2008 was $26.2 million). The Company does not have holdings in asset backed commercial paper.

The Company utilizes credit insurance to manage the risk associated with trade receivables. Approximately 92% of the outstanding trade receivables are covered under credit insurance. The majority of the balance is with large and financially sound customers. Accounts receivable aged greater than 90 days is $0.4 million and is considered collectable. The Company's trade receivable balance at September 30, 2009 was $24.4 million (December 31, 2008 was $18.1 million).

This increase in accounts receivable is directly related to the cancellation of a factoring arrangement at the Dresden mill as well as increased sales.

Operating Activities

Fortress operates in a cyclical industry and its operating cash flows vary accordingly. Fortress' principal operating cash expenditures are for compensation, fibre, chemicals and debt service. Operating activities provided cash of $7.9 million in the nine months ended September 30, 2009 compared to cash generation of $13.5 million in the nine months ended September 30, 2008. This change is primarily due to increased trade receivables directly related to the cancellation of a factoring arrangement at the Dresden mill.

In the third quarter of 2009, operating activities generated $8.6 million compared to $4.1 million in the prior year comparative period. The increase is due primarily to change in non-cash working capital items as well as higher net income in the current period.

Working capital is subject to cyclical operating needs, the timing of collection of receivables and the payment of payables and expenses. The CHF/CAD and Euro/CAD exchange rates were 1.0332 and 1.5686 respectively as at September 30, 2009 compared to a CHF/CAD rate of 1.1472 and a Euro/CAD rate of 1.7046 as at December 31, 2008.

Investing Activities

Investing activities in the nine months ended September 30, 2009 used cash of $7.7 million related to the purchase of plant and equipment at the mills and $0.5 million in deferred expenses. In the nine months ended September 30, 2008 investing activities used cash of $13.6 million related to the purchase of plant and equipment at the mills.

Investing activities in the third quarter of 2009 and 2008 used cash of $4.2 million and $7.2 million, respectively, primarily related to the purchase of plant and equipment at the mills.

Financing Activities

Financing activities in the nine months ended September 30, 2009 provided cash of $3.7 million primarily related to $6.0 million in additional financing partially offset by the repayment of debt and capital leases ($2.3 million). In the nine months ended September 30, 2008, financing used cash of $12.1 million primarily related to the redemption of the convertible note ($8.2 million), shares repurchased ($0.7 million) and repayment of debt and operating loans ($8.3 million) partially offset by $5.1 million in additional financing.

Financing activities in the third quarter of 2009 used cash of $0.2 million related to repayment of debt and capital leases. In the prior year comparative period financing activities used cash of net $ nil related to $1.0 million additional debt offset by shares repurchased ($0.7 million) and debt repayments ($0.3 million).

In the second quarter of 2008, the terms of the convertible debt were amended to allow for redemption by the Company prior to August 1, 2009. On May 22, 2008, the Company redeemed the convertible debt in full. The Company paid $8,176, representing the full principal amount of the Convertible Note together with the interest accrued up to August 1, 2009, and 105,000 common shares of the Company. On May 22, 2008 the shares of the Company were trading at $10.74. Of the $9,304 total consideration provided to Mercer, $951 was recorded as interest expense and $742 was recorded as a decrease in retained earnings. The amounts recorded as equity and interest expense were determined using methodology consistent with the original valuation of the components of the Convertible Note. The expense portion was calculated using the present value of future cash outflows using a 5% discount rate.

Related Party Transactions

There were no transactions with related parties during the nine month period ended September 30, 2009. In the nine month period ended September 30, 2008, the Company has paid or accrued office and administration expenses of $38 to a Company with a common director.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Foreign Currency

The Company is exposed to foreign exchange risk primarily in Euros and Swiss Francs. The Company's products are sold globally with prices denominated primarily in Euros and Swiss Francs. The majority of the Company's expenditures are denominated in Euros and Swiss Francs. In addition the Company holds financial assets and liabilities in the local operating currencies.

Outstanding Shares

The number of common shares outstanding at September 30, 2009 and the date of this report was 10,233,500. The number of options outstanding at September 30, 2009 and the date of this report was 740,175. The number of deferred share units and restricted share units outstanding at September 30, 2009 and the date of this report was 26,000 and 147,100 respectively.

Critical Accounting Estimates

The preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates are used for, but not limited to, the accounting for doubtful accounts, depreciation and amortization, asset impairments, valuation of equity investment, derivative financial instruments, allocation of purchase price of acquisitions, stock based compensation, pensions and post-retirement obligations, income taxes and contingencies. Actual results could differ from these estimates.

Changes in Accounting Policies

Effective January 1, 2009, the Company adopted the Canadian Institute of Chartered Accountants' new Handbook Section 3064, "Goodwill and Intangible Assets". This section replaces CICA Handbook Section 3062, "Goodwill and Intangible Assets", and establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of various preproduction and start-up costs and requires that these costs be expensed as incurred. The adoption of this new policy did not significantly impact the consolidated financial statements.

Conversion to International financial reporting standards (IFRS)

On February 13, 2008, the Accounting Standards Board announced that publicly accountable entities will be required to prepare financial statements in accordance with International Financial Reporting Standards (IFRS) for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. The Company will rely mainly on internal resources to ensure compliance with IFRS. The Company intends to convert to these new standards according to the timetable set for these new rules and has completed the following steps:

- Formally established a transition plan and project implementation team. The project team consists initially of members from Finance. Reporting is done to senior management and to the Audit Committee on a regular basis.

- Completed the first phase of its transition program, which included scoping to identify the significant accounting policy differences and their related areas of impact in terms of systems, procedures and financial statements.

- Commenced the second phase of the transition plan, which involves a completed design and work plan to measure the differences between IFRS and Canadian GAAP, and the impact on the financial statements, disclosures and results of operations.

The Company expects the transition to IFRS to impact financial reporting, accounting policies and business processes. The Company will continue to review all proposed and continuing projects of the International Accounting Standards Board to determine their impact and will continue to invest in training and resources throughout the transition period to facilitate a timely conversion. At this time, the impact on the Company's future financial position and results of operations is not reasonably determinable.

Internal Controls Over Financial Reporting

Based on current securities legislation in Canada, the Chief Executive Officer and the Chief Financial Officer of the Company are required to certify that they have:

- designed the Company's disclosure controls and procedures, or caused them to be designed under their supervision;

- designed the Company's internal control over financial reporting, or caused it to be designed under their supervision; and

- evaluated the effectiveness of the Company's disclosure controls and procedures and the Company's internal control over financial reporting as of September 30, 2009.

During the third quarter of 2009, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect the Company's internal control over financial reporting. An evaluation was performed under the supervision and with the participation of the Company's management including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures and the Company's internal control over financial reporting as of September 30, 2009. In addition, independent testing of the effectiveness of the Company's internal control over financial reporting as of December 31, 2008 was performed. The Company's management concluded that the Company's disclosure controls and procedures and the Company's internal control over financial reporting were effective as of September 30, 2009.

Management's Outlook

Combining the consistently positive results at Dresden this quarter with a strong quarter from Landqart due to higher margin banknote paper sales relative to prior quarters has provided Fortress with the Company's best historical quarterly EBITDA.

As the year has progressed it has become apparent that our mills have been able to endure the economic crisis and produce healthy results further strengthening our balance sheet at a time the company is evaluating internal growth initiatives and accretive acquisition opportunities.

The Company is encouraged by the results at our Dresden mill and the Company expects to utilize the increased capacity to meet current and forecasted demand and strengthen our position in the global non-woven wallpaper market. The efficiency enhancements at our Dresden mill will enable us to meet some of the challenges resulting from current economic conditions.

The market for security papers continues to show strength and the order book for wallpaper base has grown to its current level of eight weeks.

Risks and Uncertainties

A comprehensive discussion of Risk Factors is included in the Company's 2008 annual information form available on SEDAR at www.sedar.com.

Selected Quarterly Information

(thousands of dollars, except per unit amounts, earnings per share ("EPS"), exchange rates and shares outstanding, unaudited)	Q3 2009	Q2 2009	Q1 2009	Q4 2008
Sales	51,000	49,638	46,623	46,331
Operating income	5,198	4,460	3,765	4,399
EBITDA	6,967	5,699	5,032	5,966
Net income	3,467	1,926	3,584	2,778
Basic EPS	$0.34	$0.19	$0.35	$0.27
Diluted EPS	$0.34	$0.19	$0.35	$0.27
Weighted average shares outstanding Basic (thousands)	10,234	10,234	10,234	10,235
Weighted average shares outstanding Diluted (thousands)	10,296	10,234	10,234	10,235
Average Swiss/Canadian exchange rate[(1)]	1.0335	1.0498	1.0845	1.0470
Average Euro/Canadian exchange rate [(1)]	1.5699	1.5891	1.6226	1.5960

(thousands of dollars, except per unit amounts, earnings per share ("EPS"), exchange rates and shares outstanding, unaudited)	Q3 2008	Q2 2008	Q1 2008	Q4 2007
Sales	43,744	49,138	49,789	37,537
Operating income	4,993	5,075	5,527	3,380
EBITDA	6,234	6,184	6,643	4,255
Net income	2,312	3,401	4,189	2,279
Basic EPS	$0.22	$0.33	$0.41	$0.22
Diluted EPS	$0.22	$0.33	$0.38	$0.22
Weighted average shares outstanding Basic (thousands)	10,302	10,248	10,203	10,204
Weighted average shares outstanding Diluted (thousands)	10,471	10,423	11,141	11,141
Average Swiss/Canadian exchange rate[(1)]	0.9699	0.9797	0.9405	0.8563
Average Euro/Canadian exchange rate [(1)]	1.5623	1.5778	1.5046	1.4213

(1) Source – Bank of Canada (average noon rate for the period)

FORTRESS PAPER LTD.
CONSOLIDATED BALANCE SHEETS
(Canadian dollars, amounts in thousands, unaudited)

	As at September 30, 2009	As at December 31, 2008
ASSETS		
Current		
Cash and cash equivalents	$ 28,368	$ 26,187
Trade accounts receivable	24,405	18,108
Other accounts receivable	3,052	3,846
Inventories	30,033	31,968
Prepaid expenses	222	373
	86,080	80,482
Restricted cash	46	49
Deferred expenses	488	–
Property, plant and equipment	47,460	43,536
Employee future benefits *(note 4)*	10,193	11,574
Total assets	$ 144,267	$ 135,641
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	$ 23,980	$ 24,502
Income taxes payable	4,465	5,455
Current portion of long-term debt *(note 5)*	6,939	6,831
	35,384	36,788
Long-term debt *(note 5)*	24,244	23,760
Future income taxes	1,927	2,187
Total liabilities	$ 61,555	$ 62,735
Shareholders' equity *(note 6)*		
Share capital	59,083	59,083
Contributed surplus	2,936	2,107
Retained earnings	20,693	11,716
Total shareholders' equity	82,712	72,906
Total liabilities and shareholders' equity	$ 144,267	$ 135,641

(See accompanying notes)

Approved by the Board of Directors:

"Chadwick Wasilenkoff" — Director

"Richard Whittall" — Director

FORTRESS PAPER LTD.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME AND RETAINED EARNINGS (DEFICIT)
(Canadian dollars, amounts in thousands, unaudited)

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Sales	$ 51,000	$ 43,744	$ 147,261	$ 142,671
Costs and expenses				
Cost of products sold	(38,352)	(31,600)	(113,033)	(106,925)
Amortization	(1,350)	(865)	(3,446)	(2,338)
Selling, general and administration	(5,681)	(5,910)	(16,530)	(16,685)
Stock-based compensation *(note 7)*	(419)	(376)	(829)	(1,128)
Operating income	5,198	4,993	13,423	15,595
Other				
Interest, net	(276)	(42)	(725)	(1,180)
Foreign exchange loss	(365)	(1,257)	(76)	(484)
Net Income before income taxes	4,557	3,694	12,622	13,931
Income tax expense	(1,090)	(1,382)	(3,645)	(4,029)
Net income and comprehensive income	$ 3,467	$ 2,312	$ 8,977	$ 9,902
Earnings per share				
Basic	$ 0.34	$ 0.22	$ 0.88	$ 0.97
Diluted	$ 0.34	$ 0.22	$ 0.88	$ 0.96
Weighted average number of shares outstanding				
Basic	10,233,500	10,302,343	10,233,500	10,251,701
Diluted	10,295,590	10,471,179	10,254,348	10,339,060

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Retained earnings (deficit)				
Balance — beginning of period	$17,226	$ 6,626	$ 11,716	$ (222)
Redemption of Convertible Note *(note 5)*	–	–	–	(742)
Earnings	3,467	2,312	8,977	9,902
Balance — end of period	$ 20,693	$ 8,938	$ 20,693	$ 8,938

(See accompanying notes)

FORTRESS PAPER LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Canadian dollars, amounts in thousands, unaudited)

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Cash flows from operating activities				
Net income	$ 3,467	$ 2,312	$ 8,977	$ 9,902
Items not affecting cash:				
Amortization	1,350	865	3,446	2,338
Future income taxes	(83)	(72)	(260)	(635)
Foreign exchange (gain) loss on long term debt	(1,150)	(1,442)	(3,097)	1,673
Foreign exchange loss on operating loan	-	-	-	256
Foreign exchange loss (gain) on cash and cash equivalents	648	1,345	1,253	(732)
Stock based compensation	419	376	829	1,128
	4,651	3,384	11,148	13,930
Non-operating interest penalty *(note 5)*	-	-	-	950
Change in non-cash working capital items				
Accounts receivable	3,292	2,593	(5,503)	(596)
Inventories	422	(807)	1,935	(2,617)
Prepaid expenses	125	25	151	162
Employee future benefits	439	379	1,380	(1,078)
Accounts payable and other	(367)	(1,460)	(1,207)	2,784
	8,564	4,114	7,904	13,535
Cash flows from financing activities				
Shares repurchased *(note 6)*	-	(661)	-	(661)
Redemption of Convertible Note, including penalties *(note 5)*	-	-	-	(8,176)
Repayment of long-term debt	(170)	(157)	(2,119)	(1,242)
Proceeds from long-term debt	-	1,006	6,041	5,130
Repayment of operating loans	-	-		(6,110)
Payment on capital leases	(76)	(200)	(232)	(1,059)
	(246)	(12)	3,690	(12,118)
Cash flows from investing activities				
Additions to property, plant and equipment	(4,192)	(7,221)	(7,675)	(13,588)
Deferred expenses	(12)	-	(488)	-
Restricted cash	3	17	3	14
	(4,201)	(7,204)	(8,160)	(13,574)
Increase (decrease) in cash position	4,117	(3,102)	3,434	(12,157)
Foreign exchange (loss) gain on cash and cash equivalents	(648)	(1,345)	(1,253)	732
Cash and cash equivalents, beginning of period	24,899	38,329	26,187	45,307
Cash and cash equivalents, end of period	$ 28,368	$ 33,882	$ 28,368	$ 33,882

Supplementary cash flow information *(note 10)*

(See accompanying notes)

1. NATURE OF OPERATIONS

Fortress Paper Ltd. (the "Company") was incorporated on May 30, 2006 under the laws of the Province of British Columbia. From the date of incorporation to July 31, 2006 the Company was inactive. The Company's fiscal year end is December 31.

These unaudited interim financial statements do not include all of the disclosures required by Canadian generally accepted accounting principles ("Canadian GAAP") for annual financial statements and, accordingly, should be read in conjunction with the consolidated financial statements and notes as at and for the year ended December 31, 2008 (available on SEDAR at www.sedar.com). These unaudited interim financial statements follow the same accounting policies and methods of their application as December 31, 2008 consolidated financial statements except as disclosed in Note 2.

2. CHANGE IN ACCOUNTING POLICY

Effective January 1, 2009, the Company adopted the Canadian Institute of Chartered Accountants' new Handbook Section 3064, "Goodwill and Intangible Assets". This section replaces CICA Handbook Section 3062, "Goodwill and Intangible Assets", and establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of various preproduction and start-up costs and requires that these costs be expensed as incurred. The adoption of this new policy did not significantly impact the consolidated financial statements.

3. NEW ACCOUNTING PRONOUNCEMENTS

In 2007, the Canadian Accounting Standards Board announced that Canadian generally accepted accounting principles will cease to exist for all publicly accountable enterprises targeted for fiscal years commencing January 1, 2011. From that date onward, publicly traded companies and certain other publicly accountable enterprises will be required to report under International Financial Reporting Standards ("IFRS"). The impact of the transition to IFRS on the Company's consolidated financial statements has not yet been determined.

In January 2009, the CICA issued three new standards which may affect the financial disclosures and results of operations of the Company for interim and annual periods beginning January 1, 2011 with earlier adoption permitted. CICA Handbook Section 1582, "Business Combinations", is effective for business combinations taking place after this section is adopted. CICA Handbook Section 1601, "Consolidated Financial Statements", and CICA Handbook Section 1602, "Non-controlling Interests", must be adopted at the same time as Section 1582. These Sections replace the former CICA Handbook Section 1581, "Business Combinations" and CICA Handbook Section 1600, "Consolidated Financial Statements", and establish a new Section for accounting for non-controlling interests in a subsidiary. The Company is still considering the impact of these new standards and when they will be adopted.

4. EMPLOYEE FUTURE BENEFITS

Defined benefit pension expenses of $380 and $1,165 were recorded for the three and nine month periods ended September 30, 2009. Defined benefit pension expenses of $129 and $389 were recorded for the three and nine month periods ended September 30, 2008.

(Unaudited, Canadian dollars, amounts in thousands except share and per share data)

5. LONG-TERM DEBT AND OPERATING LOANS

Long-term debt

	September 30, 2009	December 31, 2008
Credit agreements with bank maturing 2009 and 2013; interest at 2.65% and 4.5% secured by current assets (EUR 3,469 and 2008 - 962)	$ 5,442	$ 1,640
Credit agreements with bank maturing 2010, and 2011; interest at 2.75%, 2.3% and 3.8% secured by mortgage (CHF 3,650 and 2008 - 3,950)	3,771	4,532
Credit agreement with bank maturing 2012; interest at 4.8% unsecured (CHF 5,495 and 2008 - 6,280)	5,677	7,204
Credit agreements with bank maturing 2009, 2011, 2013 and 2018; interest up to 3.1% and 5.9% secured by fixed assets (CHF 15,210 and 2008 - 14,244)	15,715	16,340
Capital leases; interest at 4.7% (CHF nil and 2008 - 19)	-	21
Capital leases; interest at 4.0% (EUR 368 and 2008 - 501)	578	854
	31,183	30,591
Less: Current portion	(6,939)	(6,831)
	$ 24,244	$ 23,760

Operating loans

During 2008 the Company fully repaid and closed its operating loans.

Convertible note

During the nine month period ended September 30, 2008 the Company redeemed in full a convertible note in the principal amount of $7,500 with a maturity date of August 2011. The Company had initially recorded a liability portion of $6,900 and an equity portion of $600 in contributed surplus. The liability portion was calculated using present value of future cash outflows using a 10% discount rate.

The Company paid $8,176, representing the full principal amount of the convertible note together with the interest accrued up to August 1, 2009, and 105,000 common shares of the Company. On May 22, 2008, the date of redemption, the shares of the Company were trading at $10.74. Of the $9,304 total consideration provided, $950 was recorded as interest expense and $742 was recorded as a decrease in retained earnings. The amounts recorded as equity and interest expense were determined using methodology consistent with the original valuation of the components of the convertible note. The expense portion was calculated using the present value of future cash outflows using a 5% discount rate.

(Unaudited, Canadian dollars, amounts in thousands except share and per share data)

6. SHAREHOLDERS' EQUITY

(a) **Authorized:**

Unlimited number of common shares without par value
Unlimited number of preferred shares with par value $1,000

(b) **Issued and fully paid — common shares**:

	Number of Shares	Share Capital	Contributed Surplus
Balance, December 31, 2007	10,203,500	$ 58,428	$ 1,508
Stock based compensation	—	—	1,388
Share repurchase	(75,000)	(473)	(189)
Shares issued on redemption of Convertible Note *(note 5)*	105,000	1,128	(600)
Balance, December 31, 2008	10,233,500	$ 59,083	$ 2,107
Stock based compensation	—	—	829
Balance, September 30, 2009	10,233,500	$ 59,083	$ 2,936

Share Repurchase

During 2008 the Company repurchased and cancelled 75,000 of its own common shares through a normal course issuer bid for a total cost of $661.

7. STOCK BASED COMPENSATION

During 2006 the Company adopted a stock incentive plan. The exercise price of options granted under the Stock Option Plan shall be as determined by the Board of Directors when such options are granted, subject to any limitations imposed by any relevant stock exchange or regulatory authority.

At the Company's Annual General Meeting held April 30, 2009 shareholders approved a long term incentive plan which provides for the grant of restricted share units, performance share units and deferred share units to key employees and directors of the Company. The aggregate number of shares issuable under the long-term incentive plan in respect of awards, together with shares reserved for issuance under all of the Company's other security-based compensation arrangements, shall not exceed ten (10) percent of the Company's issued and outstanding shares.

(Unaudited, Canadian dollars, amounts in thousands except share and per share data)

Stock Options

In June 2009, options were granted for 35,000 shares which vest over two years to an employee and officer of the Company. The weighted average fair vale of the options granted during 2009 was estimated at $2.98 per option (2008 - $2.57) at the grant date using the Black Scholes option pricing model. Option pricing models require the input of highly subjective assumptions including the expected volatility. Changes in the assumptions can materially affect the fair value estimate, and, therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Company's stock options. Assumptions used in the pricing model are as follows:

	2009	**2008**
Risk free interest rate	1.78%	4%
Expected life of options	5 years	5 years
Annualized volatility	53%	40%
Dividend rate	Nil	Nil

During the second quarter of 2009 options for 307,500 shares, held by directors and officers of the Company were cancelled.

Stock option transactions and the number of stock options outstanding are summarised as follows:

	Number of options	**Exercise Price**
Balance, December 31, 2007	982,675	$ 8.00
Granted January 1, 2008	30,000	$ 8.00
Balance, December 31, 2008	1,012,675	$ 8.00
Cancelled May 25, 2009	(25,000)	$ 8.00
Cancelled June 10, 2009	(282,500)	8.00
Granted June 23, 2009	35,000	8.00
Balance, September 30, 2009	740,175	$ 8.00

As at September 30, 2009, 486,842 stock options were exercisable (December 31, 2008 – 535,117). No stock options were exercised during the three or nine month period ended September 30, 2009, or during the year ended December 31, 2008. The stock options issued have various vesting dates which range from one to three years from the IPO or grant dates. The weighted average remaining expected life of the stock options issued as at September 30, 2009 is 3.01 years.

Deferred Share Unit Awards

A Deferred Share Unit ("DSU") is a right granted to a non-employee director to receive one common share of the Company, from treasury, on a deferred basis. The value of the DSUs, when redeemed, is equal to the market value of the shares on the redemption date, including the value of dividends paid on the Company's common shares, if any, as if they had been reinvested in additional DSUs on each payment date. The DSUs may only be redeemed upon a director's retirement from the Company. The Company recognizes the expense at the time of grant. On August 28, 2009, non-employee directors were awarded 26,000 units in aggregate. The Company recorded $185 stock compensation expense and contributed surplus. At September 30, 2009 there were 26,000 units outstanding.

Restricted Share Unit Awards

A Restricted Share Unit ("RSU") is a right granted to a key employee to receive one common share of the Company, from treasury, on a time vested basis. The fair value of restricted share awards is determined based upon the number of shares granted and the quoted price of the Company's stock on the date of grant. Restricted shares generally vest over three years. The company recognizes the expense on a straight-line basis over the vesting period. On August 28, 2009 there were restricted share awards of 147,100 units to key employees. For the period ended September 30, 2009, $29 was recorded as stock compensation expense and contributed surplus. As at September 30, 2009, the total remaining unrecognized compensation cost related to RSUs amounted to $1,015, which will be amortized over their remaining vesting period.

8. RELATED PARTY TRANSACTIONS

There were no transactions with related parties during the nine month period ended September 30, 2009. In the nine month period ended September 30, 2008, the Company paid or accrued office and administration expenses of $38 to a Company with a common director.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

(Unaudited, Canadian dollars, amounts in thousands except share and per share data)

9. SEGMENTED INFORMATION

The segmentation of the Company's manufacturing operations by mill is based on a number of factors, including production, production processes, and economic characteristics. The Landqart mill produces specialty and security papers while the Dresden mill produces non-woven wallpaper base products. During the three month period ended September 30, 2009, the Company earned revenue from two customers representing approximately 14% and 10% of sales, respectively. No single customer accounted for 10% or more of the Company's total sales for the three months ended September 30, 2008. During the nine month period ended September 30, 2009, the Company earned revenue from one customer representing approximately 10% of sales. No single customer accounted for 10% or more of the Company's total sales for the nine months ended September 30, 2008.

	Three months ended September 30, 2009			
	Dresden Mill (Germany)	**Landqart Mill** (Switzerland)	**Corporate** (Canada)	**Fortress Paper Consolidated**
Sales	$ 27,011	23,989	—	$ 51,000
Operating earnings (loss)	$ 4,661	1,844	(1,307)	$ 5,198
Amortization	$ (553)	(797)	—	$ (1,350)
Stock-based compensation[1]	$ —	—	(419)	$ (419)
Capital expenditures	$ 3,243	1,070	—	$ 4,313
Property, plant and equipment	$ 19,367	28,093	—	$ 47,460
Sales by geographic area	%	%		%
Germany	43.5	16.9		31.0
Switzerland	—	13.3		6.3
Other Western Europe	20.6	58.6		38.5
Eastern Europe	33.6	5.9		20.6
Other	2.3	5.3		3.7
Total	100.0	100.0	—	100.0

[1]Stock-based compensation is included in operating earnings (loss)

	Three months ended September 30, 2008			
	Dresden Mill (Germany)	**Landqart Mill** (Switzerland)	**Corporate** (Canada)	**Fortress Paper Consolidated**
Sales	$ 24,664	19,080	—	$ 43,744
Operating earnings (loss)	$ 4,874	1,195	(1,076)	$ 4,993
Amortization	$ (481)	(384)	—	$ (865)
Stock-based compensation[2]	$ —	—	(376)	$ (376)
Capital expenditures	$ 3,854	3,012	—	$ 6,866
Property, plant and equipment	$ 15,574	26,148	—	$ 41,722
Sales by geographic area	%	%		%
Germany	54.6	19.0		39.6
Switzerland	—	28.1		11.9
Other Western Europe	21.1	36.1		27.4
Eastern Europe	23.3	7.7		16.7
Other	1.0	9.1		4.4
Total	100.0	100.0	-	100.0

[2]Stock-based compensation is included in operating earnings (loss)

(Unaudited, Canadian dollars, amounts in thousands except share and per share data)

	Nine months ended September 30, 2009			
	Dresden Mill (Germany)	**Landqart Mill** (Switzerland)	**Corporate** (Canada)	**Fortress Paper Consolidated**
Sales	$ 82,050	65,211	—	$ 147,261
Operating earnings (loss)	$ 14,172	2,712	(3,461)	$ 13,423
Amortization	$ (1,656)	(1,790)	—	$ (3,446)
Stock-based compensation[1]	$ —	—	(829)	$ (829)
Capital expenditures	$ 4,371	3,000	—	$ 7,371
Property, plant and equipment	$ 19,367	28,093	—	$ 47,460
Sales by geographic area	%	%		%
Germany	43.9	15.5		31.3
Switzerland	—	21.1		9.3
Other Western Europe	23.8	49.3		35.1
Eastern Europe	30.4	5.7		19.5
Other	1.9	8.4		4.8
Total	100.0	100.0	—	100.0

[1]Stock-based compensation is included in operating earnings (loss)

	Nine months ended September 30, 2008			
	Dresden Mill (Germany)	**Landqart Mill** (Switzerland)	**Corporate** (Canada)	**Fortress Paper Consolidated**
Sales	$ 82,867	59,804	—	$ 142,671
Operating earnings (loss)	$ 15,851	2,767	(3,023)	$ 15,595
Amortization	$ (1,224)	(1,114)	—	$ (2,338)
Stock-based compensation[1]	$ —	—	(1,128)	$ (1,128)
Capital expenditures	$ 6,292	7,141	—	$ 13,433
Property, plant and equipment	$ 15,574	26,148	—	$ 41,722
Sales by geographic area	%	%		%
Germany	52.3	16.5		37.4
Switzerland	—	22.9		9.5
Other Western Europe	23.7	37.7		29.5
Eastern Europe	22.0	11.3		17.6
Other	2.0	11.6		6.0
Total	100.0	100.0	—	100.0

[2]Stock-based compensation is included in operating earnings (loss)

(Unaudited, Canadian dollars, amounts in thousands except share and per share data)

10. SUPPLEMENTARY CASH FLOW INFORMATION

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Interest paid	$ 267	$ 40	$ 731	$ 1,401
Income taxes paid	926	2,847	4,487	2,947

Non cash items

Non cash property, plant and equipment purchases included in accounts payable increased by $121 for the three months ended September 30, 2009 and decreased by $355 for the three months ended September 30, 2008.

Non cash property, plant and equipment purchases included in accounts payable decreased by $304 for the nine months ended September 30, 2009 and increased by $154 for the nine months ended September 30, 2008.

During the three months ended June 30, 2008 there were 105,000 common shares of the Company issued as part of the redemption of the Convertible Note (note 5).