

RAYONIER INC  
Form 10-Q  
April 24, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**  
**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended March 31, 2008

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

COMMISSION FILE NUMBER 1-6780

**RAYONIER INC.**

**Incorporated in the State of North Carolina**

**I.R.S. Employer Identification Number 13-2607329**

**50 North Laura Street, Jacksonville, FL 32202**

**(Principal Executive Office)**

**Telephone Number: (904) 357-9100**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

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Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

As of April 18, 2008, there were outstanding 78,437,236 Common Shares of the Registrant.

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**RAYONIER INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
**AND COMPREHENSIVE INCOME**

(Unaudited)

(Dollars in thousands, except per share data)

|   | <b>Three Months Ended</b> |             |
|---|---------------------------|-------------|
|   | <b>March 31,</b>          |             |
|   | <b>2008</b>               | <b>2007</b> |
| <b>SALES</b>  | \$ 284,193                | \$ 299,729  |
| Costs and Expenses  |                           |             |
| Cost of sales   | 211,012                   | 231,742     |
| Selling and general expenses  | 14,944                    | 15,845      |
| Other operating income, net   | (1,286)                   | (2,995)     |
|   | 224,670                   | 244,592     |
| Equity in income of New Zealand joint venture   | 972                       | 23          |
| <b>OPERATING INCOME</b>   | 60,495                    | 55,160      |
| Interest expense  | (11,198)                  | (13,619)    |
| Interest and miscellaneous income, net  | 1,501                     | 1,013       |
| <b>INCOME BEFORE INCOME TAXES</b>   | 50,798                    | 42,554      |
| Provision for income taxes  | (10,247)                  | (7,474)     |
| <b>NET INCOME</b>   | 40,551                    | 35,080      |
| <b>OTHER COMPREHENSIVE INCOME (LOSS)</b>  |                           |             |
| Foreign currency translation adjustment   | 4,097                     | (857)       |
| Amortization of pension and postretirement costs, net of tax provision of \$561 and \$561 | 1,346                     | 1,324       |
| <b>COMPREHENSIVE INCOME</b>   | \$ 45,994                 | \$ 35,547   |
| <b>EARNINGS PER COMMON SHARE</b>  |                           |             |
| Basic earnings per share  | \$ 0.52                   | \$ 0.45     |
| Diluted earnings per share  | \$ 0.51                   | \$ 0.45     |

See Notes to Condensed Consolidated Financial Statements.

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**RAYONIER INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

(Unaudited)

(Dollars in thousands)

|  | March 31,<br>2008 | December 31,<br>2007 |
|--|-------------------|----------------------|
| <b>ASSETS</b>  |                   |                      |
| <b>CURRENT ASSETS</b>  |                   |                      |
| Cash and cash equivalents  | \$ 146,869        | \$ 181,081           |
| Accounts receivable, less allowance for doubtful accounts of \$677 and \$677 | 80,127            | 81,068               |
| Inventory  |                   |                      |
| Finished goods   | 59,882            | 63,083               |
| Work in process  | 7,431             | 9,188                |
| Raw materials  | 7,374             | 10,122               |
| Manufacturing and maintenance supplies                                       | 2,049             | 1,898                |
| Total inventory  | 76,736            | 84,291               |
| Other current assets   | 47,360            | 49,780               |
| Total current assets   | 351,092           | 396,220              |
| <b>TIMBER AND TIMBERLANDS, NET OF DEPLETION AND AMORTIZATION</b>             | 1,122,292         | 1,117,219            |
| <b>PROPERTY, PLANT AND EQUIPMENT</b>   |                   |                      |
| Land   | 25,287            | 25,282               |
| Buildings  | 124,078           | 124,030              |
| Machinery and equipment  | 1,212,133         | 1,190,852            |
| Total property, plant and equipment  | 1,361,498         | 1,340,164            |
| Less-accumulated depreciation  | (1,006,835)       | (994,409)            |
|  | 354,663           | 345,755              |
| <b>INVESTMENT IN JOINT VENTURE</b>   | 68,822            | 62,766               |
| <b>OTHER ASSETS</b>  | 151,872           | 157,081              |
|  | \$ 2,048,741      | \$ 2,079,041         |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                                  |                   |                      |
| <b>CURRENT LIABILITIES</b>   |                   |                      |
| Accounts payable   | \$ 72,861         | \$ 66,224            |
| Bank loans and current maturities  | 585               | 55,585               |
| Accrued taxes  | 14,183            | 7,179                |
| Accrued payroll and benefits   | 20,607            | 30,065               |
| Accrued interest   | 13,436            | 3,481                |
| Accrued customer incentives  | 10,734            | 12,350               |
| Other current liabilities  | 38,210            | 33,460               |
| Current liabilities for dispositions and discontinued operations (Note 10)   | 10,154            | 10,069               |

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|   |              |              |
|---|--------------|--------------|
| Total current liabilities   | 180,770      | 218,413      |
| <b>LONG-TERM DEBT</b>   | 694,259      | 694,259      |
| <b>NON-CURRENT LIABILITIES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS (Note 10)</b>                 | 102,371      | 103,616      |
| <b>PENSION AND OTHER POSTRETIREMENT BENEFITS (Note 12)</b>  | 67,716       | 67,217       |
| <b>OTHER NON-CURRENT LIABILITIES</b>  | 13,952       | 14,439       |
| <b>COMMITMENTS AND CONTINGENCIES (Notes 9 and 11)</b>   |              |              |
| <b>SHAREHOLDERS EQUITY</b>  |              |              |
| Common shares, 120,000,000 shares authorized, 78,430,685 and 78,216,696 shares issued and outstanding | 489,198      | 487,407      |
| Retained earnings   | 520,670      | 519,328      |
| Accumulated other comprehensive loss  | (20,195)     | (25,638)     |
|   | 989,673      | 981,097      |
|   | \$ 2,048,741 | \$ 2,079,041 |

See Notes to Condensed Consolidated Financial Statements.

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)****(Dollars in thousands)**

|   | <b>Three Months Ended<br/>March 31,</b> |                 |
|---|---|-----------------|
|   | <b>2008</b>                             | <b>2007</b>     |
| <b>OPERATING ACTIVITIES</b>                               |   |                 |
| Net income  | \$ 40,551                               | \$ 35,080       |
| Non-cash items included in income:                        |   |                 |
| Depreciation, depletion and amortization                  | 33,503                                  | 40,945          |
| Non-cash cost of real estate sold                         | 2,566                                   | 1,394           |
| Non-cash stock-based incentive compensation expense       | 3,729                                   | 4,751           |
| Deferred income tax provision (benefit)                   | 3,786                                   | (1,689)         |
| Excess tax benefits on stock-based compensation           | (954)                                   | (2,178)         |
| Other   | 1,411                                   | 1,840           |
| Decrease (increase) in accounts receivable                | 941                                     | (3,541)         |
| Decrease in inventory                                     | 3,845                                   | 16,516          |
| Increase (decrease) in accounts payable                   | 2,684                                   | (11,657)        |
| Decrease (increase) in other current assets               | 77                                      | (15,819)        |
| Increase (decrease) in accrued liabilities                | 10,718                                  | (13,831)        |
| (Decrease) increase in other non-current liabilities      | (69)                                    | 2,796           |
| (Increase) decrease in other assets                       | (781)                                   | 367             |
| Expenditures for dispositions and discontinued operations | (1,771)                                 | (2,572)         |
| <b>CASH PROVIDED BY OPERATING ACTIVITIES</b>              | <b>100,236</b>                          | <b>52,402</b>   |
| <b>INVESTING ACTIVITIES</b>                               |   |                 |
| Capital expenditures                                      | (31,831)                                | (31,376)        |
| Purchase of timberlands and wood chipping facilities      | (19,567)                                | (8,670)         |
| Decrease (increase) in restricted cash                    | 10,013                                  | (14,037)        |
| Other   | 3,153                                   | 7,219           |
| <b>CASH USED FOR INVESTING ACTIVITIES</b>                 | <b>(38,232)</b>                         | <b>(46,864)</b> |
| <b>FINANCING ACTIVITIES</b>                               |   |                 |
| Issuance of debt  |   | 80,000          |
| Repayment of debt   | (55,000)                                | (68,000)        |
| Dividends paid  | (39,128)                                | (36,300)        |
| Repurchase of common shares                               | (3,488)                                 |                 |
| Issuance of common shares                                 | 596                                     | 5,051           |
| Excess tax benefits on stock-based compensation           | 954                                     | 2,178           |
| <b>CASH USED FOR FINANCING ACTIVITIES</b>                 | <b>(96,066)</b>                         | <b>(17,071)</b> |
| <b>EFFECT OF EXCHANGE RATE CHANGES ON CASH</b>            | <b>(150)</b>                            | <b>(167)</b>    |
| <b>CASH AND CASH EQUIVALENTS</b>                          |   |                 |
| Decrease in cash and cash equivalents                     | (34,212)                                | (11,700)        |

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|                            |            |           |
|----------------------------|------------|-----------|
| Balance, beginning of year | 181,081    | 40,171    |
| Balance, end of period     | \$ 146,869 | \$ 28,471 |

**SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION  
AND NONCASH INVESTING ACTIVITIES:**

|   |           |           |
|---|-----------|-----------|
| Cash paid (received) during the period: |           |           |
| Interest                                | \$ 641    | \$ 20,230 |
| Income taxes                            | \$ (262)  | \$ 6,755  |
| Non-cash investing activity:            |           |           |
| Capital assets purchased on account     | \$ 14,037 | \$ 15,950 |

See Notes to Condensed Consolidated Financial Statements.



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**RAYONIER INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(Dollars in thousands unless otherwise stated)**

**1. BASIS OF PRESENTATION**

The unaudited condensed consolidated financial statements of Rayonier Inc. and its subsidiaries (Rayonier or the Company), reflect all adjustments (which include normal recurring adjustments) necessary for a fair presentation of the results of operations, financial position and cash flows for the periods presented. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of certain estimates by management in determining the amount of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. There are risks inherent in estimating; therefore, actual results could differ from those estimates. For a full description of the Company's significant accounting policies, please refer to the Notes to Consolidated Financial Statements in the 2007 Annual Report on Form 10-K.

***New Accounting Standards***

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements* (SFAS 157). This Standard defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. It applies to other accounting pronouncements where the FASB requires or permits fair value measurements but does not require any new fair value measurements. In February 2008, FASB issued FASB Staff Position (FSP) No. 157-2, *Effective Date of FASB Statement No. 157*, which delayed the effective date of SFAS 157 for certain non-financial assets and non-financial liabilities to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. The Company adopted SFAS 157 for financial assets and liabilities on January 1, 2008. It did not have any impact on the Company's results of operations or financial position and did not result in any additional disclosures. The Company is in the process of evaluating the effect, if any, the adoption of FSP No. 157-2 will have on its results of operations or financial position.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities- Including an amendment of FASB Statement No. 155* (SFAS 159). This statement permits entities to choose to measure selected assets and liabilities at fair value. The Company adopted SFAS 159 on January 1, 2008 resulting in no impact to the Company's financial condition, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations* (SFAS 141(R)). This statement establishes how the acquiring entity recognizes and measures the identifiable assets, the liabilities assumed and the goodwill acquired in a business combination. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008. The Company has not determined the impact, if any, the statement will have on its financial condition, results of operations or cash flows.

In December 2007, FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements - an amendment of ARB No. 51* (SFAS 160). SFAS 160 is effective for fiscal years beginning after December 15, 2008. This statement addresses changes to noncontrolling interests (more commonly known as minority interests) which is the portion of equity in a subsidiary not attributable to the parent entity. Presently, the Company does not have any non-controlling interests. Therefore, the Company currently believes that the impact of SFAS 160, if any, will primarily depend on the materiality of non-controlling interests arising in future transactions, including those entered into during 2008, to which the financial statement presentation and disclosure provisions of SFAS 160 will apply.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133* (SFAS 161). This Statement requires enhanced disclosures about an entity's derivative and hedging activities, including (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The Company is in the process of evaluating the effect, if any, the adoption of SFAS 161 will have on its financial statements.



**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****(Dollars in thousands unless otherwise stated)****2. INCOME PER COMMON SHARE**

The following table provides details of the calculation of basic and diluted earnings per common share:

|   | Three Months Ended<br>March 31, |            |
|---|---------------------------------|------------|
|   | 2008                            | 2007       |
| Net income  | \$ 40,551                       | \$ 35,080  |
| Shares used for determining basic earnings per common share   | 78,254,220                      | 77,130,711 |
| Dilutive effect of:   |                                 |            |
| Stock options   | 705,050                         | 1,107,394  |
| Performance and restricted shares                             | 253,017                         | 290,116    |
| Shares used for determining diluted earnings per common share | 79,212,287                      | 78,528,221 |
| Basic earnings per common share:                              |                                 |            |
| Net income  | \$ 0.52                         | \$ 0.45    |
| Diluted earnings per common share:                            |                                 |            |
| Net income  | \$ 0.51                         | \$ 0.45    |

**3. INCOME TAXES**

Rayonier qualifies as a real estate investment trust ( REIT ) under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended ( the Code ). In general, only the Company ' s taxable REIT subsidiaries (which operate the Company ' s non-REIT qualified businesses) are subject to U.S. federal and state corporate income taxes. However, the Company is subject to U.S. corporate income tax on built-in gains (the excess of fair market value over tax basis for property held by the Company upon REIT election at January 1, 2004) on taxable sales of such property during the first 10 years following its election to be taxed as a REIT. Accordingly, no provision has been made for U.S. corporate income taxes, except for current and deferred taxes on certain property sales and on income from taxable REIT subsidiary operations. In addition, the Company is subject to foreign tax on non-U.S. operations.

***Prohibited Transactions***

As a REIT, the Company can be subject to a 100 percent tax on the gain resulting from prohibited transactions. The Company believes it has not engaged in any prohibited transactions since it elected REIT status.

***Like-Kind Exchanges***

Under current tax law, the built-in gain tax from the sale of REIT property can be eliminated if sale proceeds from relinquished properties are reinvested in similar property consistent with the requirements of the Code regarding like-kind exchanges (LKE), so long as the replacement property is owned at least until expiration of the 10 year built-in gain period (10 year period which began on January 1, 2004). However, this

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does not restrict the Company's ability to harvest timber on a pay-as-cut basis from such replacement property during the 10 year built-in gain period.

### ***Undistributed Foreign Earnings***

The Company has undistributed foreign earnings from its non-U.S. operations, which it intends to permanently reinvest overseas. The Company also intends to reinvest all future foreign earnings overseas. Therefore, no U.S. corporate income taxes have been provided on undistributed foreign earnings.

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****(Dollars in thousands unless otherwise stated)****3. INCOME TAXES (Continued)*****Provision for Income Taxes***

The Company's effective tax rate, before discrete item(s), increased from 16.7 percent in the first quarter of 2007 to 20.5 percent in the first quarter of 2008. The rate increased primarily due to proportionately higher earnings from the Company's taxable REIT subsidiary. Including discrete items, the effective tax rate was 20.2 percent in first quarter 2008 versus 17.6 percent in the prior year quarter.

The Company's effective tax rate is below the 35 percent U.S. statutory tax rate primarily due to tax benefits associated with being a REIT and LKE transactions. Partially offsetting these benefits is the loss of tax deductibility on interest expense (\$1.4 million in first quarter 2008) and corporate overhead expenses associated with REIT activities (\$2.5 million in first quarter 2008). The net tax benefit from REIT activities for first quarter 2008 was \$7.7 million compared to \$7.6 million in the prior year period. The Company recognized \$2.9 million in LKE tax benefits during the first quarter of 2008 compared to \$1.0 million in the first quarter of 2007.

The following table reconciles the Company's income tax provision at the U.S. statutory tax rate to the reported provision and effective tax rate (millions of dollars):

|  | <b>Three months ended</b> |          |             |          |
|--|---------------------------|----------|-------------|----------|
|  | <b>March 31,</b>          |          |             |          |
|  | <b>2008</b>               | <b>%</b> | <b>2007</b> | <b>%</b> |
| Income tax provision at U.S. statutory rate          | \$ (17.8)                 | (35.0)   | \$ (14.9)   | (35.0)   |
| State and local income taxes, net of federal benefit | (0.6)                     | (1.2)    | (0.3)       | (0.7)    |
| REIT income not subject to federal tax               | 7.7                       | 15.1     | 7.6         | 18.0     |
| Permanent differences/other                          | 0.3                       | 0.6      | 0.5         | 1.0      |
| Income tax provision before discrete items           | \$ (10.4)                 | (20.5)   | \$ (7.1)    | (16.7)   |
| Other  | 0.2                       | 0.3      | (0.4)       | (0.9)    |
| Income tax provision as reported                     | \$ (10.2)                 | (20.2)   | \$ (7.5)    | (17.6)   |

***Tax Audits***

The following table provides detail of the tax years that remain subject to examination by the Internal Revenue Service ( IRS ) and other significant taxing jurisdictions:

| <b>Taxing Jurisdiction</b>    | <b>Open Tax Periods</b> |      |
|-------------------------------|-------------------------|------|
| U.S. Internal Revenue Service | 2005                    | 2008 |
| State of Florida              | 2003                    | 2008 |
| State of Georgia              | 2003                    | 2008 |
| State of Alabama              | 2004                    | 2008 |
| New Zealand Inland Revenue    | 2003                    | 2008 |

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The Company is currently at the IRS appeals level related to one matter from the tax year 2003 and has other matters under review by various taxing authorities, including the examination of tax years 2005 and 2006 by the IRS. The Company believes its reported tax positions are technically sound and its uncertain tax position liabilities at March 31, 2008 adequately reflect the probable resolution of these items.

### ***FIN 48 Disclosures***

There were no significant changes to the Company's uncertain tax positions in the first quarter of 2008. For a detail of the Company's uncertain tax positions, please refer to Note 9 *Income Taxes* in the 2007 Annual Report on Form 10-K.

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## RAYONIER INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(Dollars in thousands unless otherwise stated)

**4. RESTRICTED DEPOSITS**

In order to qualify for LKE treatment, cash proceeds from real estate sales must be deposited with a third party intermediary and accounted for as restricted cash until qualifying replacement property is acquired. In the event that LKE purchases are not completed, the proceeds are returned to the Company and reclassified as cash after 180 days. As of March 31, 2008 and December 31, 2007, the Company had \$0 and \$10.0 million, respectively, of proceeds from real estate sales classified as restricted cash in Other assets, which were on deposit with an LKE intermediary.

**5. SHAREHOLDERS EQUITY**

An analysis of shareholders equity for the three months ended March 31, 2008 and the year ended December 31, 2007 is shown below:

| (Share and per share amounts not in thousands)   | Common Shares |            | Retained Earnings | Accumulated Other Comprehensive Loss | Shareholders Equity |
|--|---------------|------------|-------------------|--------------------------------------|---------------------|
|  | Shares        | Amount     |                   |                                      |                     |
| <b>Balance, December 31, 2006</b>                | 76,879,826    | \$ 450,636 | \$ 495,988        | \$ (28,646)                          | \$ 917,978          |
| Net income                                       |               |            | 174,269           |                                      | 174,269             |
| Dividends (\$1.94 per share)                     |               |            | (150,929)         |                                      | (150,929)           |
| Issuance of shares under incentive stock plans   | 1,412,781     | 18,891     |                   |                                      | 18,891              |
| Stock-based compensation expense                 |               | 13,478     |                   |                                      | 13,478              |
| Warrants and hedge, net                          |               | (355)      |                   |                                      | (355)               |
| Excess tax benefit on stock-based compensation   |               | 7,907      |                   |                                      | 7,907               |
| Repurchase of common shares                      | (75,911)      | (3,150)    |                   |                                      | (3,150)             |
| Net loss from pension and postretirement plans   |               |            |                   | (3,997)                              | (3,997)             |
| Foreign currency translation adjustment          |               |            |                   | 7,005                                | 7,005               |
| <b>Balance, December 31, 2007</b>                | 78,216,696    | \$ 487,407 | \$ 519,328        | \$ (25,638)                          | \$ 981,097          |
| Net income                                       |               |            | 40,551            |                                      | 40,551              |
| Dividends (\$0.50 per share)                     |               |            | (39,209)          |                                      | (39,209)            |
| Issuance of shares under incentive stock plans   | 293,219       | 596        |                   |                                      | 596                 |
| Stock-based compensation expense                 |               | 3,729      |                   |                                      | 3,729               |
| Excess tax benefit on stock-based compensation   |               | 954        |                   |                                      | 954                 |
| Repurchase of common shares                      | (79,230)      | (3,488)    |                   |                                      | (3,488)             |
| Amortization of pension and postretirement costs |               |            |                   | 1,346                                | 1,346               |
| Foreign currency translation adjustment          |               |            |                   | 4,097                                | 4,097               |
| <b>Balance, March 31, 2008</b>                   | 78,430,685    | \$ 489,198 | \$ 520,670        | \$ (20,195)                          | \$ 989,673          |

**6. JOINT VENTURE INVESTMENT**

The Company holds a 40 percent interest in a joint venture (JV) that owns approximately 343,000 acres of New Zealand timberlands. Rayonier's investment in the JV is accounted for using the equity method of accounting. In addition to the Company having an equity investment, Rayonier

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New Zealand Limited (RNZ), a wholly-owned subsidiary of Rayonier Inc., serves as the manager of the JV forests, for which it receives a fee. Income from the JV is reported in the Timber segment as operating income since the Company manages the forests and its JV interest is an extension of its operations. While the JV is subject to New Zealand income taxes, its timber harvest operations are held within the REIT; therefore, the Company generally is not required to pay U.S. federal and state income taxes on its equity investment income.

A portion of the Company's equity method investment is recorded at historical cost which generates a difference between the book value of the Company's investment and its proportionate share of the JV's net assets. The difference represents the Company's unrecognized gain from RNZ's sale of timberlands to the JV upon formation in 2005. The deferred gain will be recognized on a straight-line basis over the estimated number of years the JV expects to harvest from the timberlands. As of March 31, 2008, eight years remain.



**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****(Dollars in thousands unless otherwise stated)****6. JOINT VENTURE INVESTMENT (Continued)**

The Company's investment in the JV was \$68.8 million and \$62.8 million at March 31, 2008 and December 31, 2007, respectively. The increase in the investment is mainly due to the change in the exchange rate between the New Zealand Dollar and the U.S. Dollar. For the three months ended March 31, 2008 and 2007, the Company's equity earnings from the JV were \$1.0 million and \$0, respectively.

**7. SEGMENT INFORMATION**

Rayonier operates in four reportable business segments as defined by SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information* (SFAS 131): Timber, Real Estate, Performance Fibers, and Wood Products. Timber sales include all activities that relate to the harvesting of timber. Real Estate sales currently include the sale of all properties, including those designated for higher and better use (HBU). The assets of the Real Estate segment include HBU property held by the Company's real estate subsidiary, TerraPointe LLC, and parcels under contract previously reported in the Timber segment. Allocations of depletion expense and non-cash costs of real estate sold are recorded when the Company sells an asset from the Timber segment. The Performance Fibers segment includes two major product lines, cellulose specialties and absorbent materials. The Wood Products segment is comprised of the Company's lumber operations. The Company's remaining operations include harvesting and selling timber acquired from third parties (log trading) and trading wood products. As permitted by SFAS 131, these operations are combined and reported in an "Other" category. Sales between operating segments are made based on fair market value, and intercompany profit or loss is eliminated in consolidation. The Company evaluates financial performance based on the operating income of the segments.

Operating income/(loss), as presented in the Condensed Consolidated Statements of Income and Comprehensive Income, is equal to segment income/(loss). Certain income/(loss) items in the Condensed Consolidated Statements of Income and Comprehensive Income are not allocated to segments. These items, which include gains/(losses) from certain asset dispositions, interest, miscellaneous income/(expense) and income tax (provision)/benefit, are not considered by Company management to be part of segment operations.

Total assets, sales, operating income (loss) and depreciation, depletion and amortization by segment including corporate were as follows:

|                     | March 31,<br>2008   | December 31,<br>2007 |
|---------------------|---------------------|----------------------|
| <b>ASSETS</b>       |                     |                      |
| Timber              | \$ 1,226,335        | \$ 1,204,253         |
| Real Estate         | 58,555              | 65,101               |
| Performance Fibers  | 467,974             | 466,909              |
| Wood Products       | 31,336              | 29,307               |
| Other Operations    | 28,073              | 29,671               |
| Corporate and other | 236,468             | 283,800              |
| <b>TOTAL</b>        | <b>\$ 2,048,741</b> | <b>\$ 2,079,041</b>  |

**Three Months Ended  
March 31,  
2008                      2007**

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| <b>SALES</b>       |                   |                   |
|--------------------|-------------------|-------------------|
| Timber             | \$ 47,199         | \$ 65,006         |
| Real Estate        | 29,351            | 20,997            |
| Performance Fibers | 174,926           | 166,381           |
| Wood Products      | 18,912            | 19,693            |
| Other Operations   | 13,805            | 27,652            |
| <b>TOTAL</b>       | <b>\$ 284,193</b> | <b>\$ 299,729</b> |

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****(Dollars in thousands unless otherwise stated)****7. SEGMENT INFORMATION (Continued)**

|                                | <b>Three Months Ended<br/>March 31,</b> |                  |
|--------------------------------|---|------------------|
|                                | <b>2008</b>                             | <b>2007</b>      |
| <b>OPERATING INCOME (LOSS)</b> |   |                  |
| Timber                         | \$ 12,019                               | \$ 26,267        |
| Real Estate                    | 21,768                                  | 15,215           |
| Performance Fibers             | 37,056                                  | 27,110           |
| Wood Products                  | (2,544)                                 | (3,328)          |
| Other Operations               | (573)                                   | (1,281)          |
| Corporate and other            | (7,231)                                 | (8,823)          |
| <b>TOTAL</b>                   | <b>\$ 60,495</b>                        | <b>\$ 55,160</b> |

|   | <b>Three Months Ended<br/>March 31,</b> |                  |
|---|---|------------------|
|   | <b>2008</b>                             | <b>2007</b>      |
| <b>DEPRECIATION, DEPLETION AND AMORTIZATION</b> |   |                  |
| Timber  | \$ 18,067                               | \$ 21,773        |
| Real Estate                                     | 2,695                                   | 2,165            |
| Performance Fibers                              | 11,164                                  | 15,320           |
| Wood Products                                   | 1,444                                   | 1,592            |
| Other Operations                                | 8                                       | 19               |
| Corporate and other                             | 125                                     | 76               |
| <b>TOTAL</b>                                    | <b>\$ 33,503</b>                        | <b>\$ 40,945</b> |

**8. FINANCIAL INSTRUMENTS***Interest Rate Swap Agreements*

Rayonier Forest Resources, L.P. (RFR), a wholly-owned subsidiary of Rayonier Inc., previously entered into two interest rate swaps on \$90 million of 8.288 percent fixed rate notes payable which matured on December 31, 2007. One swap converted interest payments from the fixed rate to six month LIBOR plus 4.99 percent on \$40 million of debt, while the second swap converted interest payments from the fixed rate to six month LIBOR plus 4.7825 percent. These swaps qualified as a fair value hedge under SFAS 133. As such, the net effect from the interest rate swaps was recorded as interest expense. The interest rate differentials on the swap agreements settled every June 30 and December 31, until maturity. During the three months ended March 31, 2007, the swap agreements increased interest expense by \$0.4 million.

*Commodity Swap Agreements*

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The Company enters into commodity forward contracts to fix some of its fuel oil and natural gas costs at its Performance Fibers mills. The Company's commodity forward contracts do not qualify for hedge accounting under SFAS 133 and instead are required to be marked-to-market.

During the three months ended March 31, 2008 and 2007, the Company realized a gain of \$0.2 million and a loss of \$0.3 million, respectively, on fuel oil forward contracts. The mark-to-market adjustments are recorded in Other operating income, net. The mark-to-market valuation on outstanding fuel oil forward contracts at March 31, 2008 resulted in an asset of \$0.2 million. At December 31, 2007, there were no outstanding fuel oil or natural gas forward contracts.

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****(Dollars in thousands unless otherwise stated)****9. GUARANTEES**

The Company provides financial guarantees as required by creditors, insurance programs and state and foreign governmental agencies. As of March 31, 2008, the following financial guarantees were outstanding:

|                               | <b>Maximum<br/>Potential<br/>Payment</b> | <b>Carrying<br/>Amount of<br/>Liability</b> |
|-------------------------------|--|---|
| Standby letters of credit (1) | \$ 71,778                                | \$ 62,493                                   |
| Guarantees (2)                | 6,408                                    | 73  |
| Surety bonds (3)              | 9,175                                    | 1,472                                       |
| Total                         | \$ 87,361                                | \$ 64,038                                   |

- (1) Approximately \$62 million of the standby letters of credit serve as credit support for industrial revenue bonds. The remaining letters of credit support obligations under various insurance related agreements, primarily workers compensation and pollution liability policy requirements. These letters of credit expire at various dates during 2008 and will be renewed as required.
- (2) In conjunction with RNZ's sale of timberlands to the New Zealand JV in October 2005, the Company guaranteed five years of Crown Forest license obligations. The JV is the primary obligor and has posted a bank performance bond with the New Zealand government. If the JV fails to pay the obligation, the New Zealand government will demand payment from the bank that posted the bond. If the bank defaults on the bond, the Company would then have to perform. As of March 31, 2008, three annual payments, of \$1.3 million each, remain. This guarantee expires in 2010.  
In conjunction with a timberland sale and note monetization in the first quarter of 2004, the Company issued a make-whole agreement pursuant to which it guaranteed \$2.5 million of obligations of a qualified special purpose entity that was established to complete the monetization. At March 31, 2008 and December 31, 2007, the Company has recorded a de minimus liability to reflect the fair market value of its obligation to perform under the make-whole agreement.
- (3) Rayonier issued surety bonds primarily to secure timber in the State of Washington and to provide collateral for the Company's workers compensation self-insurance program in that state. These surety bonds expire at various dates during 2008 and are renewed as required.

**10. LIABILITIES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS**

The Company's dispositions and discontinued operations include its Port Angeles, WA mill, which was closed in 1997; Southern Wood Piedmont Company (SWP), which ceased operations in 1989 except for investigation and remediation activities; Eastern Research Division (ERD), which ceased operations in 1981; and other miscellaneous assets held for disposition. SWP is subject to the Resource Conservation and Recovery Act (RCRA), or has been designated a potentially responsible party (PRP), or has had other claims made against it, under the U.S. Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) and/or other federal or state statutes relating to

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the investigation and remediation of environmentally-impacted sites, with respect to 10 former wood treating sites which are no longer operating.

An analysis of activity in the liabilities for dispositions and discontinued operations for the three months ended March 31, 2008 and the year ended December 31, 2007, is as follows:

|                                       | <b>March 31,<br/>2008</b> | <b>December 31,<br/>2007</b> |
|---------------------------------------|---------------------------|------------------------------|
| Balance, January 1,                   | \$ 113,685                | \$ 122,516                   |
| Expenditures charged to liabilities   | (1,771)                   | (8,575)                      |
| Additions/(reductions) to liabilities | 611                       | (256)                        |
| Balance, end of period                | 112,525                   | 113,685                      |
| Less: Current portion                 | (10,154)                  | (10,069)                     |
| Non-current portion                   | \$ 102,371                | \$ 103,616                   |

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**RAYONIER INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**(Dollars in thousands unless otherwise stated)**

**10. LIABILITIES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS (Continued)**

Rayonier has identified specific liabilities for three SWP sites (Augusta, GA, Spartanburg, SC, and East Point, GA) as material and requiring separate disclosure, which was presented in the Company's 2007 Annual Report on Form 10-K. There have not been any significant changes in these sites' liability reserves for the three months ended March 31, 2008. Rayonier accounts for environmental liabilities on an undiscounted basis. For an analysis of the activity for the three years ended December 31, 2007 and a brief description of these individually material sites, see the Company's 2007 Annual Report on Form 10-K, Note 15 to Consolidated Financial Statements.

The Company estimates that expenditures for environmental remediation, monitoring and other costs for all dispositions and discontinued operations will be approximately \$8 million in 2008 and \$10 million in 2009. Such costs will be charged against its liabilities for dispositions and discontinued operations, which include environmental investigation, remediation and monitoring costs. The Company believes established liabilities are sufficient for costs expected to be incurred over the next 20 years with respect to its dispositions and discontinued operations. Remedial actions for these sites vary, but may include, among other remedies, removal or treatment of contaminated soils, recovery and treatment/remediation of groundwater, and source remediation and/or control.

In addition, the Company is exposed to the risk of reasonably possible additional losses in excess of the established liabilities. As of March 31, 2008, this amount could range up to \$30 million and arises from uncertainty over the effectiveness of treatments, additional contamination that may be discovered, changes in applicable law and the exercise of discretion in interpretation of applicable law and regulations by governmental agencies, and in environmental remediation technology.

The reliability and precision of cost estimates for these sites and the amount of actual future environmental costs can be impacted by various factors, including but not limited to: significant changes in discharge or treatment volumes, requirements to perform additional or different remediation, changes in environmental remediation technology, the extent of groundwater contamination migration, additional findings of contaminated soil or sediment off-site, remedy selection, and the outcome of negotiations with federal and state agencies. Additionally, the potential for Brownfield (environmentally impacted site considered for re-development) treatment of a site, or other similar projects, could accelerate expenditures as well as impact the amount and/or type of remediation required, as could new laws, regulations and the exercise of discretion in interpretation of applicable law and regulations by governmental agencies. Based on information currently available, the Company does not believe that any future changes in estimates, if necessary, would materially affect its consolidated financial position or results of operations.

**11. CONTINGENCIES**

From time to time, Rayonier may become liable with respect to pending and threatened litigation and environmental and other matters. The following updates or repeats commentary included in the 2007 Annual Report on Form 10-K.

The Company has been named as a defendant in various other lawsuits and claims arising in the normal course of business. While the Company has procured reasonable and customary insurance covering risks normally occurring in connection with its businesses, it has in certain cases retained some risk through the operation of self-insurance, primarily in the areas of workers' compensation, property insurance, and general liability. These other lawsuits and claims, either individually or in the aggregate, are not expected to have a material effect on the Company's financial position, results of operations, or cash flow.

***Legal Proceedings***

**Combe Fill South** In 1998, the U.S. Environmental Protection Agency (EPA) and the New Jersey Department of Environmental Protection (DEP) filed separate lawsuits against Rayonier Inc., and approximately 30 other defendants, in the U.S. District Court, District of New Jersey,

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seeking recovery of current and future response costs and natural resource damages under applicable federal and state law relating to a contaminated landfill in Chester Township, New Jersey, referred to as Combe Fill South (Combe). It is alleged that the Company's former ERD in Whippany, New Jersey sent small quantities of dumpster waste, via a contract hauler, to Combe in the 1960s and early 1970s. The Company is working with other defendants in a joint defense group, which subsequently filed third-party actions against over 200 parties seeking contribution. A court-ordered, nonbinding alternative dispute resolution process is ongoing, and in March of 2006 a court-appointed neutral issued a report and recommendations. While settlement discussions have been active, no final agreement has been reached. The Company believes that its liabilities at March 31, 2008 adequately reflect the probable costs to be incurred upon the ultimate resolution of these matters.

Jesup Mill Consent Decree In November 2007, the Company and the Environmental Protection Division of the Georgia Department of Natural Resources (EPD) reached agreement, subject to public comment, on a consent decree that would resolve



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**RAYONIER INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**(Dollars in thousands unless otherwise stated)**

**11. CONTINGENCIES (Continued)**

certain issues relating to the color of the Jesup mill's permitted effluent discharged to the Altamaha River. Under the consent decree, Rayonier has agreed to implement a color reduction plan which will include installation of additional brown stock washing capacity (to better remove residual pulping liquors from cooked wood pulp) and oxygen delignification technology (which reduces the lignin content in the pulp prior to bleaching), spill recovery systems and modifications to certain operating practices. These projects will be completed over a seven year period pursuant to a time frame set forth in the consent decree, and the costs are expected to approximate \$75.0 million. The consent decree also provides for decreasing color limits in the mill's effluent over the seven year period as projects are completed. No citations, fines or penalties are imposed by the consent decree, except that stipulated penalties may be assessed by EPD in the event that the projects are not completed by the agreed schedule. The consent decree was published for public comment in November 2007, and on March 17, 2008, EPD executed the document as negotiated.

East Point, Georgia Notice of Violation (NOV) On March 28, 2008, SWP received an NOV and Proposed Consent Order (the "Order") from EPD relating to its East Point, Georgia site. The Order asserts that SWP violated conditions in its RCRA Part B permit, specifically related to SWP's alleged failure to report the presence of oil (referred to as DNAPL, or dense non-aqueous phase liquid) in a monitoring well. Under the terms of the Order, EPD proposed a fine of \$0.8 million and is demanding that SWP perform a facility-wide remedial investigation; also, based on such investigation, EPD has required that SWP prepare a new corrective action plan for the facility. Finally, EPD is requesting an immediate increase in SWP's financial assurance for the site to \$17.6 million from the current approximately \$4.0 million level. (Note that financial assurance is provided for SWP via a Rayonier Inc. guaranty.) The Company is conducting a factual and legal analysis of EPD's claims and intends to vigorously defend this matter. The Company believes that its liabilities at March 31, 2008 adequately reflect the probable costs to be incurred upon the ultimate resolution of these matters.

***Environmental Matters***

The Company is subject to stringent environmental laws and regulations concerning air emissions, water discharges, waste handling and disposal, and forestry operations. Such environmental laws and regulations include the Federal Clean Air Act, the Clean Water Act, RCRA, as amended, CERCLA, the Endangered Species Act, and similar state laws and regulations. Management closely monitors its environmental responsibilities, and believes that the Company is in substantial compliance with current environmental requirements. Notwithstanding Rayonier's current compliance status, many of its operations are subject to stringent and constantly evolving environmental requirements, which are often the result of legislation, regulator discretion, regulation and negotiation. As such, contingencies in this area include, without limitation:

The Company's manufacturing facilities operate in accordance with various permits, which often impose operating conditions that require significant expenditures to ensure compliance. Upon renewal and renegotiation of these permits, the issuing agencies often seek to impose new or additional conditions, which could adversely affect the Company's operations and financial performance.

As environmental laws and regulations change, and regulatory administrative and judicial interpretations of new and existing laws and regulations are made, the Company's operations may be adversely affected.

In Rayonier's forestry operations, federal, state and local laws and regulations intended to protect threatened and endangered animal and plant species and their habitat, as well as wetlands and waterways, limit, and in some cases may prevent, timber harvesting, road construction and other activities on private lands. For example, Washington, where the Company holds approximately 431,000 acres of timberlands, has among the most stringent forestry laws and regulations in the country.

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Environmental requirements relating to real estate development, and especially in respect of wetland delineation and mitigation, stormwater management, drainage, waste disposal, and potable water supply and protection, may significantly impact the size, scope, timing, and financial returns of the Company's projects. Moreover, multiple permits are often required for a project, and may involve a lengthy application process.

The Company's discontinued operations with historical environmental contamination are subject to a number of federal, state, and local laws. As these requirements change over time, they may mandate more stringent levels of soil and groundwater investigation, remediation, and monitoring. While management believes that the Company's current estimates are adequate, future changes to these legal requirements could adversely affect the cost and timing of its activities on these sites.

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****(Dollars in thousands unless otherwise stated)**

Over time, the complexity and stringency of environmental laws and regulations have increased significantly, and the cost of compliance with these laws and regulations has also increased. In general, management believes these trends will continue.

It is the opinion of management that substantial expenditures will be required over the next 10 years in the area of environmental compliance. See Note 10 *Liabilities for Dispositions and Discontinued Operations* for additional information regarding the Company's environmental liabilities.

**12. EMPLOYEE BENEFIT PLANS**

The Company has four qualified non-contributory defined benefit pension plans, which collectively cover substantially all employees hired prior to January 2006, and an unfunded plan that provides benefits in excess of amounts allowable under current tax law in the qualified plans. Employee benefit plan liabilities are calculated using actuarial estimates and management assumptions. These estimates are based on historical information, along with certain assumptions about future events. Changes in assumptions, as well as changes in actual experience, could cause the estimates to change.

The net periodic benefit cost for the Company's pension and postretirement plans (medical and life insurance) for the three months ended March 31, 2008 and 2007 are shown in the following table:

|  | <b>Pension</b>            |                 | <b>Postretirement</b>     |                 |
|--|---------------------------|-----------------|---------------------------|-----------------|
|  | <b>Three Months Ended</b> |                 | <b>Three Months Ended</b> |                 |
|  | <b>March 31,</b>          |                 | <b>March 31,</b>          |                 |
|  | <b>2008</b>               | <b>2007</b>     | <b>2008</b>               | <b>2007</b>     |
| <b>Components of Net Periodic Benefit Cost</b> |                           |                 |                           |                 |
| Service cost                                   | \$ 1,586                  | \$ 1,606        | \$ 164                    | \$ 155          |
| Interest cost                                  | 3,824                     | 3,245           | 628                       | 562             |
| Expected return on plan assets                 | (4,817)                   | (4,110)         |                           |                 |
| Amortization of prior service cost             | 329                       | 363             | 179                       | 179             |
| Amortization of losses                         | 1,118                     | 1,011           | 281                       | 332             |
| <b>Net periodic benefit cost</b>               | <b>\$ 2,040</b>           | <b>\$ 2,115</b> | <b>\$ 1,252</b>           | <b>\$ 1,228</b> |

The Company does not have any required pension plan contributions for 2008 and has not made any discretionary pension contributions during the three months ended March 31, 2008.

**13. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

Accumulated Other Comprehensive Income (Loss) was comprised of the following as of March 31, 2008 and December 31, 2007:

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|   | March 31,<br>2008  | December 31,<br>2007 |
|---|--------------------|----------------------|
| Foreign currency translation adjustments                      | \$ 38,394          | \$ 34,297            |
| Unrecognized components of employee benefit plans, net of tax | (58,589)           | (59,935)             |
| <b>Total</b>  | <b>\$ (20,195)</b> | <b>\$ (25,638)</b>   |

During the three months ended March 31, 2008, the increase in net foreign currency translation adjustments was due to the change in the New Zealand to U.S. dollar exchange rate. Amortization of unrecognized components of employee pension and postretirement plan expense of \$1.3 million was recognized during the three months ended March 31, 2008.

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## RAYONIER INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Dollar amounts in thousands unless otherwise stated)

**14. CONSOLIDATING FINANCIAL STATEMENTS**

In October 2007, Rayonier TRS Holdings Inc. (TRS), a wholly-owned subsidiary of Rayonier Inc., issued \$300 million of 3.75% Senior Exchangeable Notes due 2012. The notes are guaranteed by Rayonier Inc. and are non-callable. In connection with this offering, the Company is providing the following condensed consolidating financial information in accordance with SEC Regulation S-X Rule 3-10, *Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered*. Each entity in the consolidating financial information follows the same accounting policies as described in the consolidated financial statements, except for the use of the equity method of accounting to reflect ownership interests in 100 percent owned subsidiaries which are eliminated upon consolidation and the allocation of certain expenses of Rayonier Inc., incurred for the benefit of its subsidiaries.

**Condensed Consolidating Statements of Income  
For the Three Months Ended March 31, 2008**

|  | Rayonier Inc.<br>(Parent<br>Guarantor) | Rayonier TRS<br>Holdings<br>Inc.<br>(Issuer) | Subsidiaries of<br>Rayonier TRS<br>Holdings Inc.<br>(Non-guarantors) | All Other<br>Subsidiaries<br>(Non-guarantors) | Consolidating<br>Adjustments | Total<br>Consolidated |
|--|--|--|--|---|------------------------------|-----------------------|
| <b>SALES</b>   | \$                                     | \$   | \$ 228,846   | \$ 92,692                                     | \$ (37,345)                  | \$ 284,193            |
| Costs and Expenses                                   |  |  |  |   |                              |                       |
| Cost of sales  |  |  | 188,715  | 33,756  | (11,459)                     | 211,012               |
| Selling and general expenses                         | 2,526                                  |  | 11,664   | 754   |                              | 14,944                |
| Other operating (income) expense, net                | (202)                                  |  | 695  | (1,779)                                       |                              | (1,286)               |
|  | 2,324                                  |  | 201,074  | 32,731  | (11,459)                     | 224,670               |
| Equity in income (loss) of New Zealand joint venture | 1,024                                  |  | (52)   |   |                              | 972                   |
| <b>OPERATING (LOSS) INCOME</b>                       | (1,300)                                |  | 27,720   | 59,961  | (25,886)                     | 60,495                |
| Interest income (expense)                            | 536                                    | (3,139)                                      | (6,616)  | (1,979)                                       |                              | (11,198)              |
| Interest and miscellaneous income (expense), net     | 887                                    | (773)  | 33   | 1,354   |                              | 1,501                 |
| Equity in income from subsidiaries                   | 40,957                                 | 9,952  |  |   | (50,909)                     |                       |
| <b>INCOME BEFORE INCOME TAXES</b>                    | 41,080                                 | 6,040  | 21,137   | 59,336  | (76,795)                     | 50,798                |
| Income tax (provision) benefit                       | (529)                                  | 1,467  | (11,185)   |   |                              | (10,247)              |
| <b>NET INCOME</b>                                    | \$ 40,551                              | \$ 7,507                                     | \$ 9,952   | \$ 59,336                                     | \$ (76,795)                  | \$ 40,551             |

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(Dollar amounts in thousands unless otherwise stated)

**14. CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

|  | Condensed Consolidating Statements of Income<br>For the Three Months Ended March 31, 2007 |  |  |   |                              |                       |
|--|---|--|--|---|------------------------------|-----------------------|
|  | Rayonier Inc.<br>(Parent<br>Guarantor)  | Rayonier TRS<br>Holdings<br>Inc.<br>(Issuer) | Subsidiaries of<br>Rayonier TRS<br>Holdings Inc.<br>(Non-guarantors) | All Other<br>Subsidiaries<br>(Non-guarantors) | Consolidating<br>Adjustments | Total<br>Consolidated |
| <b>SALES</b>   | \$  | \$   | \$ 238,706   | \$ 67,565                                     | \$ (6,542)                   | \$ 299,729            |
| Costs and Expenses                                   |   |  |  |   |                              |                       |
| Cost of sales  | (20)  |  | 205,027  | 33,669  | (6,934)                      | 231,742               |
| Selling and general expenses                         | 3,735   |  | 11,311   | 799   |                              | 15,845                |
| Other operating income, net                          | (17)  |  | (1,608)  | (1,370)                                       |                              | (2,995)               |
|  |   | 3,698  | 214,730  | 33,098  | (6,934)                      | 244,592               |
| Equity in (loss) income of New Zealand joint venture | (348)   |  | 371  |   |                              | 23                    |
| <b>OPERATING (LOSS) INCOME</b>                       | (4,046)   |  | 24,347   | 34,467  | 392                          | 55,160                |
| Interest expense                                     | (98)  |  | (8,623)  | (4,898)                                       |                              | (13,619)              |
| Interest and miscellaneous income (expense), net     | 523   |  | (900)  | 1,390   |                              | 1,013                 |
| Equity in income from subsidiaries                   | 39,785  | 9,395  |  |   | (49,180)                     |                       |
| <b>INCOME BEFORE INCOME TAXES</b>                    | 36,164  | 9,395  | 14,824   | 30,959  | (48,788)                     | 42,554                |
| Income tax provision                                 | (1,084)   |  | (5,429)  |   | (961)                        | (7,474)               |
| <b>NET INCOME</b>                                    | \$ 35,080   | \$ 9,395                                     | \$ 9,395   | \$ 30,959                                     | \$ (49,749)                  | \$ 35,080             |

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(Dollar amounts in thousands unless otherwise stated)

**14. CONSOLIDATING FINANCIAL STATEMENTS (Continued)**Condensed Consolidating Balance Sheets  
As of March 31, 2008

|  | Rayonier Inc.<br>(Parent<br>Guarantor) | Rayonier TRS<br>Holdings<br>Inc.<br>(Issuer) | Subsidiaries of<br>Rayonier TRS<br>Holdings Inc.<br>(Non-guarantors) | All Other<br>Subsidiaries<br>(Non-guarantors) | Consolidating<br>Adjustments | Total<br>Consolidated |
|--|--|--|--|---|------------------------------|-----------------------|
| <b>ASSETS</b>  |  |  |  |   |                              |                       |
| <b>CURRENT ASSETS</b>  |  |  |  |   |                              |                       |
| Cash and cash equivalents  | \$ (306)                               | \$   | \$ 139,480   | \$ 7,695                                      | \$                           | \$ 146,869            |
| Accounts receivable, less allowance for<br>doubtful accounts         | 623                                    |  | 71,856   | 8,376   | (728)                        | 80,127                |
| Inventory  |  |  | 79,961   |   | (3,225)                      | 76,736                |
| Intercompany interest receivable                                     |  |  |  | 1,029   | (1,029)                      |                       |
| Other current assets   | 11,577                                 |  | 31,949   | 3,834   |                              | 47,360                |
| Total current assets   | 11,894                                 |  | 323,246  | 20,934  | (4,982)                      | 351,092               |
| <b>TIMBER AND TIMBERLANDS, NET OF<br/>DEPLETION AND AMORTIZATION</b> |  |  |  |   |                              |                       |
|  | 1,808                                  |  | 40,409   | 1,080,075                                     |                              | 1,122,292             |
| <b>NET PROPERTY, PLANT AND<br/>EQUIPMENT</b>                         |  |  |  |   |                              |                       |
|  | 1,999                                  |  | 351,197  | 1,467   |                              | 354,663               |
| INVESTMENT IN JOINT VENTURE  | 95,544                                 |  | (26,722)   |   |                              | 68,822                |
| INVESTMENT IN SUBSIDIARIES   | 929,226                                | 473,181                                      |  |   | (1,402,407)                  |                       |
| INTERCOMPANY/NOTES RECEIVABLE  | 38,466                                 |  |  | 10,746  | (49,212)                     |                       |
| OTHER ASSETS   | 29,306                                 | 17,960                                       | 420,450  | 3,615   | (319,459)                    | 151,872               |
| <b>TOTAL ASSETS</b>  | <b>\$ 1,108,243</b>                    | <b>\$ 491,141</b>                            | <b>\$ 1,108,580</b>  | <b>\$ 1,116,837</b>                           | <b>\$ (1,776,060)</b>        | <b>\$ 2,048,741</b>   |
| <b>LIABILITIES AND SHAREHOLDERS<br/>EQUITY</b>                       |  |  |  |   |                              |                       |
| <b>CURRENT LIABILITIES</b>   |  |  |  |   |                              |                       |
| Accounts payable   | \$ 3,896                               | \$   | \$ 67,734  | \$ 1,231                                      | \$                           | \$ 72,861             |
| Bank loans and current maturities                                    |  |  | 585  |   |                              | 585                   |
| Accrued taxes  | 116                                    | (3,673)                                      | 14,480   | 3,260   |                              | 14,183                |
| Accrued payroll and benefits   | 8,227                                  |  | 11,145   | 1,235   |                              | 20,607                |
| Accrued interest   | 21                                     | 5,156  | 6,940  | 1,319   |                              | 13,436                |
| Accrued customer incentives  |  |  | 10,734   |   |                              | 10,734                |
| Other current liabilities  | 11,903                                 |  | 15,511   | 12,189  | (1,393)                      | 38,210                |
| Current liabilities for dispositions and<br>discontinued operations  |  |  | 10,154   |   |                              | 10,154                |
| Total current liabilities  | 24,163                                 | 1,483  | 137,283  | 19,234  | (1,393)                      | 180,770               |
| <b>LONG-TERM DEBT</b>  |  |  |  |   |                              |                       |
|  |  | 300,000                                      | 341,680  | 52,579  |                              | 694,259               |
|  |  |  | 102,371  |   |                              | 102,371               |

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NON-CURRENT LIABILITIES FOR  
DISPOSITIONS AND DISCONTINUED  
OPERATIONS

|  |              |            |              |              |                |              |
|--|--------------|------------|--------------|--------------|----------------|--------------|
| PENSION AND OTHER<br>POSTRETIREMENT BENEFITS | 68,122       |            | (406)        |              |                | 67,716       |
| OTHER NON-CURRENT LIABILITIES                | 9,938        |            | 3,414        | 18,708       | (18,108)       | 13,952       |
| INTERCOMPANY PAYABLE                         | 16,347       |            | 51,057       | 40,574       | (107,978)      |              |
| TOTAL LIABILITIES                            | 118,570      | 301,483    | 635,399      | 131,095      | (127,479)      | 1,059,068    |
| TOTAL SHAREHOLDERS EQUITY                    | 989,673      | 189,658    | 473,181      | 985,742      | (1,648,581)    | 989,673      |
| TOTAL LIABILITIES AND<br>SHAREHOLDERS EQUITY | \$ 1,108,243 | \$ 491,141 | \$ 1,108,580 | \$ 1,116,837 | \$ (1,776,060) | \$ 2,048,741 |



**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(Dollar amounts in thousands unless otherwise stated)

**14. CONSOLIDATING FINANCIAL STATEMENTS (Continued)****Condensed Consolidating Balance Sheets  
As of December 31, 2007**

|  | <b>Rayonier<br/>Inc. (Parent<br/>Guarantor)</b> | <b>Rayonier TRS<br/>Holdings<br/>Inc.<br/>(Issuer)</b> | <b>Subsidiaries of<br/>Rayonier TRS<br/>Holdings Inc.<br/>(Non-guarantors)</b> | <b>All Other<br/>Subsidiaries<br/>(Non-guarantors)</b> | <b>Consolidating<br/>Adjustments</b> | <b>Total<br/>Consolidated</b> |
|--|---|--|--|--|--------------------------------------|-------------------------------|
| <b>ASSETS</b>  |   |  |  |  |                                      |                               |
| <b>CURRENT ASSETS</b>  |   |  |  |  |                                      |                               |
| Cash and cash equivalents  | \$ 4,211  | \$   | \$ 173,029   | \$ 3,841   | \$                                   | \$ 181,081                    |
| Accounts receivable, less allowance for doubtful accounts        | 217   |  | 79,142   | 1,709  |                                      | 81,068                        |
| Inventory  |   |  | 88,979   |  | (4,688)                              | 84,291                        |
| Intercompany interest receivable                                 |   |  |  | 1,137  | (1,137)                              |                               |
| Other current assets   | 12,823  |  | 32,226   | 4,731  |                                      | 49,780                        |
| Total current assets   | 17,251  |  | 373,376  | 11,418   | (5,825)                              | 396,220                       |
| <b>TIMBER AND TIMBERLANDS, NET OF DEPLETION AND AMORTIZATION</b> |   |  |  |  |                                      |                               |
|  | 1,819   |  | 36,015   | 1,079,385  |                                      | 1,117,219                     |
| <b>NET PROPERTY, PLANT AND EQUIPMENT</b>                         |   |  |  |  |                                      |                               |
|  | 2,147   |  | 342,173  | 1,435  |                                      | 345,755                       |
| INVESTMENT IN JOINT VENTURE                                      | 89,933  |  | (27,167)   |  |                                      | 62,766                        |
| INVESTMENT IN SUBSIDIARIES                                       | 918,269   | 494,063  |  |  | (1,412,332)                          |                               |
| INTERCOMPANY/NOTES RECEIVABLE                                    | 53,397  |  | 12,851   | 14,819   | (81,067)                             |                               |
| OTHER ASSETS   | 28,692  | 18,772   | 386,762  | 13,260   | (290,405)                            | 157,081                       |
| <b>TOTAL ASSETS</b>  | <b>\$ 1,111,508</b>                             | <b>\$ 512,835</b>                                      | <b>\$ 1,124,010</b>  | <b>\$ 1,120,317</b>                                    | <b>\$ (1,789,629)</b>                | <b>\$ 2,079,041</b>           |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                       |   |  |  |  |                                      |                               |
| <b>CURRENT LIABILITIES</b>                                       |   |  |  |  |                                      |                               |
| Accounts payable   | \$ 3,123  | \$   | \$ 60,673  | \$ 2,428   | \$                                   | \$ 66,224                     |
| Bank loans and current maturities                                |   |  | 585  | 55,000   |                                      | 55,585                        |
| Accrued taxes  | 109   | (1,687)  | 6,483  | 2,274  |                                      | 7,179                         |
| Accrued payroll and benefits                                     | 18,339  |  | 11,726   |  |                                      | 30,065                        |
| Accrued interest   |   | 2,370  | 1,100  | 11   |                                      | 3,481                         |
| Accrued customer incentives                                      |   |  | 12,350   |  |                                      | 12,350                        |
| Other current liabilities  | 11,719  |  | 12,598   | 9,143  |                                      | 33,460                        |
| Current liabilities for dispositions and discontinued operations |   |  | 10,069   |  |                                      | 10,069                        |
| Total current liabilities  | 33,290  | 683  | 115,584  | 68,856   |                                      | 218,413                       |
| <b>LONG-TERM DEBT</b>  |   |  |  |  |                                      |                               |
|  |   | 300,000  | 341,680  | 52,579   |                                      | 694,259                       |
|  |   |  | 103,616  |  |                                      | 103,616                       |

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NON-CURRENT LIABILITIES FOR  
DISPOSITIONS AND DISCONTINUED  
OPERATIONS

|  |              |            |              |              |                |              |
|--|--------------|------------|--------------|--------------|----------------|--------------|
| PENSION AND OTHER<br>POSTRETIREMENT BENEFITS | 67,606       |            | (389)        |              |                | 67,217       |
| OTHER NON-CURRENT LIABILITIES                | 10,333       |            | 3,521        | 16,987       | (16,402)       | 14,439       |
| INTERCOMPANY PAYABLE                         | 19,182       |            | 65,935       | 55,486       | (140,603)      |              |
| TOTAL LIABILITIES                            | 130,411      | 300,683    | 629,947      | 193,908      | (157,005)      | 1,097,944    |
| TOTAL SHAREHOLDERS EQUITY                    | 981,097      | 212,152    | 494,063      | 926,409      | (1,632,624)    | 981,097      |
| TOTAL LIABILITIES AND<br>SHAREHOLDERS EQUITY | \$ 1,111,508 | \$ 512,835 | \$ 1,124,010 | \$ 1,120,317 | \$ (1,789,629) | \$ 2,079,041 |

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(Dollar amounts in thousands unless otherwise stated)

**14. CONSOLIDATING FINANCIAL STATEMENTS (Continued)****Condensed Consolidating Statements of Cash Flows  
For the Three Months Ended March 31, 2008**

|   | <b>Rayonier Inc.<br/>(Parent<br/>Guarantor)</b> | <b>Rayonier TRS<br/>Holdings<br/>Inc.<br/>(Issuer)</b> | <b>Subsidiaries of<br/>Rayonier TRS<br/>Holdings Inc.<br/>(Non-guarantors)</b> | <b>All Other<br/>Subsidiaries<br/>(Non-guarantors)</b> | <b>Consolidating<br/>Adjustments</b> | <b>Total<br/>Consolidated</b> |
|---|---|--|--|--|--------------------------------------|-------------------------------|
| <b>OPERATING ACTIVITIES</b>                               |   |  |  |  |                                      |                               |
| Net income  | \$ 40,551                                       | \$ 7,507   | \$ 9,952   | \$ 59,336  | \$ (76,795)                          | \$ 40,551                     |
| Non-cash items included in income:                        |   |  |  |  |                                      |                               |
| Equity in income from investments in subsidiaries         | (40,957)  | (9,952)  |  |  | 50,909                               |                               |
| Depreciation, depletion and amortization                  |   |  | 13,395   | 21,624   | (1,516)                              | 33,503                        |
| Non-cash cost of real estate sold                         |   |  | 751  | 2,735  | (920)                                | 2,566                         |
| Non-cash stock-based incentive compensation expense       | 1,417   |  | 2,312  |  |                                      | 3,729                         |
| Deferred income tax provision (benefit)                   | 6   | (519)  | 4,299  |  |                                      | 3,786                         |
| Excess tax benefits on stock-based compensation           |   |  | (954)  |  |                                      | (954)                         |
| Other   | (639)   |  | 2,050  |  |                                      | 1,411                         |
| Dividends from investments in subsidiaries                | 30,000  | 30,000   |  |  | (60,000)                             |                               |
| (Increase) decrease in accounts receivable                | (405)   |  | 7,285  | (6,667)  | 728                                  | 941                           |
| Decrease in inventory                                     |   |  | 3,845  |  |                                      | 3,845                         |
| Increase (decrease) in accounts payable                   | 773   |  | 2,378  | (467)  |                                      | 2,684                         |
| Decrease (increase) in other current assets               | 1,246   |  | (2,063)  | 894  |                                      | 77                            |
| (Decrease) increase in accrued liabilities                | (9,906)   | 1,838  | 13,603   | 5,911  | (728)                                | 10,718                        |
| Increase (decrease) in other non-current liabilities      | 121   |  | (205)  | 1,721  | (1,706)                              | (69)                          |
| (Increase) decrease in other assets                       | (6,012)   | 293  | (24,860)   | (230)  | 30,028                               | (781)                         |
| Change in intercompany accounts                           | 6,308   |  | (11,242)   | 4,934  |                                      |                               |
| Expenditures for dispositions and discontinued operations |   |  | (1,771)  |  |                                      | (1,771)                       |
| <b>CASH PROVIDED BY OPERATING ACTIVITIES</b>              | <b>22,503</b>                                   | <b>29,167</b>  | <b>18,775</b>  | <b>89,791</b>  | <b>(60,000)</b>                      | <b>100,236</b>                |
| <b>INVESTING ACTIVITIES</b>                               |   |  |  |  |                                      |                               |
| Capital expenditures                                      |   |  | (22,321)   | (9,510)  |                                      | (31,831)                      |
| Purchase of timberlands and wood chipping facilities      |   |  | (3,857)  | (15,710)   |                                      | (19,567)                      |
| Decrease in restricted cash                               |   |  |  | 10,013   |                                      | 10,013                        |
| Investment In Subsidiaries                                |   | 833  |  |  | (833)                                |                               |
| Other   |   |  | 3,883  | (730)  |                                      | 3,153                         |
| <b>CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES</b>   |   | <b>833</b>   | <b>(22,295)</b>  | <b>(15,937)</b>  | <b>(833)</b>                         | <b>(38,232)</b>               |

| <b>FINANCING ACTIVITIES</b>                      |          |          |            |          |        |            |
|--|----------|----------|------------|----------|--------|------------|
| Repayment of debt                                |          |          |            | (55,000) |        | (55,000)   |
| Dividends paid                                   | (39,128) |          |            |          |        | (39,128)   |
| Issuance of common shares                        | 596      |          |            |          |        | 596        |
| Excess tax benefits on stock-based compensation  |          |          | 954        |          |        | 954        |
| Repurchase of common shares                      | (3,488)  |          |            |          |        | (3,488)    |
| Repayment of intercompany notes                  | 15,000   |          |            | (15,000) |        |            |
| Distributions to / from Parent                   |          | (30,000) | (30,833)   |          | 60,833 |            |
| <b>CASH USED FOR FINANCING ACTIVITIES</b>        | (27,020) | (30,000) | (29,879)   | (70,000) | 60,833 | (96,066)   |
| <b>EFFECT OF EXCHANGE RATE CHANGES ON CASH</b>   |          |          | (150)      |          |        | (150)      |
| <b>CASH AND CASH EQUIVALENTS</b>                 |          |          |            |          |        |            |
| (Decrease) increase in cash and cash equivalents | (4,517)  |          | (33,549)   | 3,854    |        | (34,212)   |
| Balance, beginning of year                       | 4,211    |          | 173,029    | 3,841    |        | 181,081    |
| Balance, end of period                           | \$ (306) | \$       | \$ 139,480 | \$ 7,695 | \$     | \$ 146,869 |

**Table of Contents****RAYONIER INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(Dollar amounts in thousands unless otherwise stated)

**14. CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

| <b>Condensed Consolidating Statements of Cash Flows</b>   |                           |                                   |   |                               |                                  |                           |
|---|---------------------------|-----------------------------------|---|-------------------------------|----------------------------------|---------------------------|
| <b>For the Three Months Ended March 31, 2007</b>          |                           |                                   |   |                               |                                  |                           |
|   | <b>Rayonier Inc.</b>      | <b>Rayonier TRS Holdings Inc.</b> | <b>Subsidiaries of Rayonier TRS Holdings Inc.</b> | <b>All Other Subsidiaries</b> | <b>Consolidating Adjustments</b> | <b>Total Consolidated</b> |
|   | <b>(Parent Guarantor)</b> | <b>(Issuer)</b>                   | <b>(Non-guarantors)</b>                           | <b>(Non-guarantors)</b>       |                                  |                           |
| <b>OPERATING ACTIVITIES</b>                               |                           |                                   |   |                               |                                  |                           |
| Net income  | \$ 35,080                 | \$ 9,395                          | \$ 9,395  | \$ 30,959                     | \$ (49,749)                      | \$ 35,080                 |
| Non-cash items included in income:                        |                           |                                   |   |                               |                                  |                           |
| Equity in income from investments in subsidiaries         | (39,785)                  | (9,395)                           |   |                               | 49,180                           |                           |
| Depreciation, depletion and amortization                  |                           |                                   | 17,687  | 23,258                        |                                  | 40,945                    |
| Non-cash cost of real estate sold                         |                           |                                   | 943   | 842                           | (391)                            | 1,394                     |
| Non-cash stock-based incentive compensation expense       | 1,948                     |                                   | 2,803   |                               |                                  | 4,751                     |
| Deferred income tax benefit                               | (692)                     |                                   | (997)   |                               |                                  | (1,689)                   |
| Excess tax benefits on stock-based compensation           |                           |                                   | (2,178)   |                               |                                  | (2,178)                   |
| Other   | 745                       |                                   | 1,095   |                               |                                  | 1,840                     |
| Dividends from investments in subsidiaries                | 30,000                    |                                   |   |                               | (30,000)                         |                           |
| Decrease (increase) in accounts receivable                | 406                       |                                   | (1,829)   | (2,118)                       |                                  | (3,541)                   |
| Decrease in inventory                                     |                           |                                   | 16,516  |                               |                                  | 16,516                    |
| Decrease in accounts payable                              | (4,840)                   |                                   | (7,025)   | (2,039)                       | 2,247                            | (11,657)                  |
| (Increase) decrease in other current assets               | (5,414)                   |                                   | (11,030)  | 625                           |                                  | (15,819)                  |
| (Decrease) increase in accrued liabilities                | (1,162)                   |                                   | (21,745)  | 8,116                         | 960                              | (13,831)                  |
| Increase (decrease) in other non-current liabilities      | 3,034                     |                                   | (234)   | 16,398                        | (16,402)                         | 2,796                     |
| Decrease (increase) in other assets                       | 2,190                     |                                   | (19,100)  | 875                           | 16,402                           | 367                       |
| Change in intercompany accounts                           | (10,782)                  |                                   | 16,662  | (5,880)                       |                                  |                           |
| Expenditures for dispositions and discontinued operations |                           |                                   | (2,572)   |                               |                                  | (2,572)                   |
| <b>CASH PROVIDED BY (USED FOR)</b>                        |                           |                                   |   |                               |                                  |                           |
| <b>OPERATING ACTIVITIES</b>                               | <b>10,728</b>             |                                   | <b>(1,609)</b>                                    | <b>71,036</b>                 | <b>(27,753)</b>                  | <b>52,402</b>             |
| <b>INVESTING ACTIVITIES</b>                               |                           |                                   |   |                               |                                  |                           |
| Capital expenditures                                      |                           |                                   | (21,448)  | (9,928)                       |                                  | (31,376)                  |
| Purchase of timberlands and wood chipping facilities      |                           |                                   | (8,670)   |                               |                                  | (8,670)                   |
| Increase in restricted cash                               |                           |                                   |   | (14,037)                      |                                  | (14,037)                  |
| Other   |                           |                                   | 7,219   |                               |                                  | 7,219                     |
| <b>CASH USED FOR INVESTING ACTIVITIES</b>                 |                           |                                   | <b>(22,899)</b>                                   | <b>(23,965)</b>               |                                  | <b>(46,864)</b>           |

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**FINANCING ACTIVITIES**

|   |          |          |          |          |
|---|----------|----------|----------|----------|
| Issuance of debt                                |          | 40,000   | 40,000   | 80,000   |
| Repayment of debt                               |          | (28,000) | (40,000) | (68,000) |
| Dividends paid                                  | (36,300) |          |          | (36,300) |
| Issuance of common shares                       | 5,051    |          |          | 5,051    |
| Excess tax benefits on stock-based compensation |          | 2,178    |          | 2,178    |
| Distributions to / from Parent                  |          |          | (30,000) | 30,000   |

**CASH (USED FOR) PROVIDED BY FINANCING ACTIVITIES**

|  |          |        |          |        |          |
|--|----------|--------|----------|--------|----------|
|  | (31,249) | 14,178 | (30,000) | 30,000 | (17,071) |
|--|----------|--------|----------|--------|----------|

**EFFECT OF EXCHANGE RATE CHANGES ON CASH**

|  |  |       |  |  |       |
|--|--|-------|--|--|-------|
|  |  | (167) |  |  | (167) |
|--|--|-------|--|--|-------|

**CASH AND CASH EQUIVALENTS**

|  |          |          |        |         |          |
|--|----------|----------|--------|---------|----------|
| (Decrease) increase in cash and cash equivalents | (20,521) | (10,497) | 17,071 | 2,247   | (11,700) |
| Balance, beginning of year                       | 28,551   | 13,867   |        | (2,247) | 40,171   |

|                        |          |          |           |    |           |
|------------------------|----------|----------|-----------|----|-----------|
| Balance, end of period | \$ 8,030 | \$ 3,370 | \$ 17,071 | \$ | \$ 28,471 |
|------------------------|----------|----------|-----------|----|-----------|

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**RAYONIER INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**(Dollars in thousands unless otherwise stated)**

**15. SUBSEQUENT EVENT**

In April 2008, the Company acquired approximately 56,300 acres of timberlands in the state of Washington for \$213 million, funding the acquisition with \$128 million of cash on hand and the remaining borrowed through the Company's existing credit facility. The timberlands acquired will increase the Company's existing holdings of merchantable Douglas fir and western hemlock timber and will be accounted for as an asset purchase.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**Safe Harbor**

When we refer to "we", "us", "our", "the Company", or "Rayonier", we mean Rayonier Inc. and its consolidated subsidiaries. References herein to "Notes" or "Financial Statements" refer to the Notes to the Condensed Consolidated Financial Statements of Rayonier Inc. included in Item 1 of this Report.

Certain statements in this document regarding anticipated financial outcomes including earnings guidance, if any, business and market conditions, outlook and other similar statements relating to Rayonier's future financial and operational performance, are "forward-looking statements" made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and other federal securities laws. These forward-looking statements are identified by the use of words such as "may", "will", "should", "expect", "estimate", "believe", "anticipate" or similar language. Forward-looking statements are not guarantees of future performance and undue reliance should not be placed on these statements.

The following important factors, among others, could cause actual results to differ materially from those expressed in forward-looking statements that may have been made in this document:

the cyclical and competitive nature of the industries in which we operate;

fluctuations in demand for, or supply of, our forest products and real estate offerings;

entry of new competitors into our markets;

changes in global economic conditions and world events, including political changes in particular regions or countries;

changes in energy and raw material prices, particularly for our performance fibers and wood products businesses;

unanticipated equipment maintenance and repair requirements at our manufacturing facilities;

the geographic concentration of a significant portion of our timberland;

our ability to identify and complete timberland acquisitions;

changes in environmental laws and regulations, including laws regarding air emissions and water discharges, remediation of contaminated sites, timber harvesting, delineation of wetlands, and endangered species, that may restrict or adversely impact our ability to conduct our business, or increase the cost of doing so;

adverse weather conditions, natural disasters and other catastrophic events such as hurricanes, wind storms and wildfires, which can adversely affect our timberlands and the production, distribution and availability of our products and raw materials such as wood, energy and chemicals;



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interest rate and currency movements;

the availability of credit generally, including its impact on the cost and terms of obtaining financing;

our capacity to incur additional debt, and any decision we may make to do so;

changes in tariffs, taxes or treaties relating to the import and export of our products or those of our competitors;

the ability to complete like-kind exchanges of property;

changes in key management and personnel;

our ability to continue to qualify as a REIT and to fund distributions using cash generated through our taxable REIT subsidiaries; and,

changes in tax laws that could reduce the benefits associated with REIT status.

In addition, specifically with respect to our Real Estate business, the following important factors, among others, could cause actual results to differ materially from those expressed in forward-looking statements that may have been made in this document:

the cyclical nature of the real estate business generally, including fluctuations in demand for both entitled and unentitled property;

the lengthy, uncertain and costly process associated with the ownership, entitlement and development of real estate, especially in Florida, which also may be affected by changes in law, policy and political factors beyond our control;

the potential for legal challenges to entitlements and permits in connection with our properties;

unexpected delays in the entry into or closing of real estate transactions;

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the existence of competing developers and communities in the markets in which we own property;

the pace of development and the rate and timing of absorption of existing entitled property in the markets in which we own property;

changes in the demographics affecting projected population growth and migration to the southeastern U.S.;

changes in environmental laws and regulations, including laws regarding water withdrawal and management and delineation of wetlands, that may restrict or adversely impact our ability to sell or develop properties;

the cost of the development of property generally, including the cost of property taxes, labor and construction materials;

the timing of construction and availability of public infrastructure; and,

the availability of financing for real estate development and mortgage loans.

**Critical Accounting Policies and Use of Estimates**

The preparation of our consolidated financial statements requires us to make estimates, assumptions and judgments that affect our assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. We base these estimates and assumptions on historical data and trends, current fact patterns, expectations and other sources of information we believe are reasonable. Actual results may differ from these estimates under different conditions. For a full description of our critical accounting policies, see Item 7 *Management's Discussion and Analysis of Financial Condition and Results of Operations* in the 2007 Annual Report on Form 10-K.

**Segment Information**

Rayonier operates in four reportable business segments as defined by SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information* (SFAS 131): Timber, Real Estate, Performance Fibers, and Wood Products. Timber sales include all activities that relate to the harvesting of timber. Real Estate sales currently include the sale of all properties, including those designated for higher and better use ( HBU ). The assets of the Real Estate segment include HBU property held by the Company's real estate subsidiary, TerraPointe LLC, and parcels under contract previously reported in the Timber segment. Allocations of depletion expense and non-cash costs of real estate sold are recorded when the Company sells an asset from the Timber segment. The Performance Fibers segment includes two major product lines, cellulose specialties and absorbent materials. The Wood Products segment is comprised of the Company's lumber operations. The Company's remaining operations include harvesting and selling timber acquired from third parties (log trading) and trading wood products. As permitted by SFAS 131, these operations are combined and reported in an Other category. Sales between operating segments are made based on fair market value, and intercompany profit or loss is eliminated in consolidation. The Company evaluates financial performance based on the operating income of the segments.

Operating income/ (loss), as presented in the Condensed Consolidated Statements of Income and Comprehensive Income, is equal to segment income/ (loss). Certain income/ (loss) items in the Condensed Consolidated Statements of Income and Comprehensive Income are not allocated to segments. These items, which include gains/(losses) from certain asset dispositions, interest, miscellaneous income/(expense) and income tax (provision)/benefit, are not considered by Company management to be part of segment operations.

**Table of Contents****Results of Operations, Three Months Ended March 31, 2008 Compared to Three Months Ended March 31, 2007**

| <b>Financial Information (in millions)</b> | <b>Three Months Ended<br/>March 31,</b> |                 |
|--|---|-----------------|
|  | <b>2008</b>                             | <b>2007</b>     |
| <b>Sales</b>                               |   |                 |
| Timber                                     | \$ 47.2                                 | \$ 65.0         |
| Real Estate                                |   |                 |
| Development                                | 0.8                                     | 3.6             |
| Rural                                      | 23.9                                    | 17.4            |
| Non-Strategic Timberlands                  | 4.7                                     |                 |
| <b>Total Real Estate</b>                   | <b>29.4</b>                             | <b>21.0</b>     |
| Performance Fibers                         |   |                 |
| Cellulose Specialties                      | 132.7                                   | 129.5           |
| Absorbent Materials                        | 42.2                                    | 36.9            |
| <b>Total Performance Fibers</b>            | <b>174.9</b>                            | <b>166.4</b>    |
| Wood Products                              | 18.9                                    | 19.7            |
| Other operations                           | 13.8                                    | 27.6            |
| <b>Total Sales</b>                         | <b>\$ 284.2</b>                         | <b>\$ 299.7</b> |
| <b>Operating Income (Loss)</b>             |   |                 |
| Timber                                     | \$ 12.0                                 | \$ 26.3         |
| Real Estate                                | 21.8                                    | 15.2            |
| Performance Fibers                         | 37.1                                    | 27.1            |
| Wood Products                              | (2.5)                                   | (3.3)           |
| Other operations                           | (0.6)                                   | (1.3)           |
| Corporate and other                        | (7.3)                                   | (8.8)           |
| <b>Total Operating Income</b>              | <b>60.5</b>                             | <b>55.2</b>     |
| Interest expense                           | (11.2)                                  | (13.6)          |
| Interest and miscellaneous income, net     | 1.5                                     | 1.0             |
| Provision for income taxes                 | (10.2)                                  | (7.5)           |
| <b>Net Income</b>                          | <b>\$ 40.6</b>                          | <b>\$ 35.1</b>  |

**Table of Contents****Timber**

| Sales (in millions)                         | 2007    | Changes Attributable to: |             |          | 2008    |
|---|---------|--------------------------|-------------|----------|---------|
|   |         | Price                    | Volume /Mix | Other    |         |
| Three months ended March 31,<br>Total Sales | \$ 65.0 | \$ (8.0)                 | \$ (9.3)    | \$ (0.5) | \$ 47.2 |

In first quarter 2008, sales were \$18 million below the prior year period as both our Eastern and Western regions experienced lower prices and volume due to the weak housing market. Average prices declined by 16 percent and 21 percent in the East and West, respectively. In the East, the decline in sawtimber prices was partially offset by an increase in pulpwood prices due to strong demand. Volumes were down 20 percent and 25 percent in the East and West, respectively, as we reduced planned harvest levels for sawlogs due to poor market conditions.

| Operating Income (in millions)                         | 2007    | Changes Attributable to: |             |             | 2008    |
|--|---------|--------------------------|-------------|-------------|---------|
|  |         | Price                    | Volume /Mix | Cost /Other |         |
| Three months ended March 31,<br>Total Operating Income | \$ 26.3 | \$ (8.0)                 | \$ (7.0)    | \$ 0.7      | \$ 12.0 |

Operating income was 54 percent below the prior year period due to lower prices and volumes resulting from the soft housing market.

**Real Estate**

| Sales (in millions)                         | 2007    | Changes Attributable to: |          |  | 2008    |
|---|---------|--------------------------|----------|--|---------|
|   |         | Price                    | Volume   |  |         |
| Three months ended March 31,<br>Development | \$ 3.6  | \$ (0.6)                 | \$ (2.2) |  | \$ 0.8  |
| Rural                                       | 17.4    | 5.1                      | 1.4      |  | 23.9    |
| Non-Strategic timberlands                   |         |                          | 4.7      |  | 4.7     |
| Total Sales                                 | \$ 21.0 | \$ 4.5                   | \$ 3.9   |  | \$ 29.4 |

| Operating Income (in millions)                         | 2007    | Changes Attributable to: |        |  | 2008    |
|--|---------|--------------------------|--------|--|---------|
|  |         | Price                    | Volume |  |         |
| Three months ended March 31,<br>Total Operating Income | \$ 15.2 | \$ 4.5                   | \$ 2.1 |  | \$ 21.8 |

Sales and operating income increased by \$8 million and \$7 million, respectively, from first quarter 2007 due to higher rural prices and volumes and non-strategic timberland sales. In 2008, we continued to experience strong interest in our rural properties and began selling non-strategic timberland holdings that did not meet our investment criteria. In first quarter 2008, we successfully completed two non-strategic timberland sales totaling 4,073 acres at an average price of \$1,158 per acre.

**Table of Contents****Performance Fibers**

| Sales (in millions)          | 2007     | Changes Attributable to: |             | 2008     |
|------------------------------|----------|--------------------------|-------------|----------|
|                              |          | Price                    | Volume /Mix |          |
| Three months ended March 31, |          |                          |             |          |
| Cellulose Specialties        | \$ 129.5 | \$ 10.7                  | \$ (7.5)    | \$ 132.7 |
| Absorbent Materials          | 36.9     | 4.7                      | 0.6         | 42.2     |
| Total Sales                  | \$ 166.4 | \$ 15.4                  | \$ (6.9)    | \$ 174.9 |

In first quarter 2008, cellulose specialties and absorbent materials prices increased by 9 percent and 13 percent from the prior year period, respectively, due to strong market demand. These price increases more than offset the 6 percent decline in cellulose specialties volume due to unplanned maintenance outages.

| Operating Income (in millions) | 2007    | Changes Attributable to: |              |          | 2008    |
|--------------------------------|---------|--------------------------|--------------|----------|---------|
|                                |         | Price                    | Volume / Mix | Costs    |         |
| Three months ended March 31,   |         |                          |              |          |         |
| Total Operating Income         | \$ 27.1 | \$ 15.4                  | \$ (1.6)     | \$ (3.8) | \$ 37.1 |

Operating income was \$10 million above the prior year period as increased prices and lower depreciation more than offset lower volume and higher maintenance, energy, wood chip and chemical costs.

**Wood Products**

| Sales (in millions)          | 2007    | Changes Attributable to: |             | 2008    |
|------------------------------|---------|--------------------------|-------------|---------|
|                              |         | Price                    | Volume /Mix |         |
| Three months ended March 31, |         |                          |             |         |
| Total Sales                  | \$ 19.7 | \$ (1.0)                 | \$ 0.2      | \$ 18.9 |

Sales were \$1 million below the prior year period as prices declined due to the soft housing market.

| Operating Loss (in millions) | 2007     | Changes Attributable to: |        | 2008     |
|------------------------------|----------|--------------------------|--------|----------|
|                              |          | Price                    | Costs  |          |
| Three months ended March 31, |          |                          |        |          |
| Total Operating Loss         | \$ (3.3) | \$ (1.0)                 | \$ 1.8 | \$ (2.5) |

First quarter 2008 operating loss improved by \$1 million from the prior year period as lower log and production costs more than offset the continuing decline in prices.

**Table of Contents*****Other Operations***

In first quarter 2008, sales were \$13.8 million compared to \$27.6 million in the prior year period. The decline in sales reflects the closure of our wood products trading business in the Northwest U.S. in May 2007. The operating loss of \$0.6 million in first quarter 2008 improved by \$0.7 million from first quarter 2007.

***Corporate and other***

Corporate expenses were \$7.3 million, down \$1.5 million from first quarter 2007 primarily due to lower stock-based and other incentive compensation expenses.

***Interest and miscellaneous income, net***

Interest expense of \$11.2 million was \$2.4 million below first quarter 2007 primarily due to lower interest rates resulting from our recent debt refinancing.

Interest and other miscellaneous income increased \$0.5 million from the prior year period primarily due to higher cash levels in 2008.

***Provision for Income Taxes***

First quarter 2008 effective tax rate before discrete items was 20.5 percent compared to 16.7 percent in first quarter 2007. The increase was due to proportionately higher earnings from our taxable REIT subsidiary. Including discrete items, the first quarter 2008 effective tax rate was 20.2 percent.

See Note 3 *Income Taxes* for additional information regarding the provision for income taxes.

***Outlook***

Due to the weak market conditions for timber and real estate, we expect that second quarter and full year 2008 earnings will be below prior year periods. However, we anticipate that the softness in those markets will be somewhat offset by the continued strength in Performance Fibers. In Real Estate, we anticipate continued interest in rural properties and non-strategic timberlands although sales will be more heavily weighted to the second half of the year. Cash available for distribution is expected to remain strong, although below 2007.

**Liquidity and Capital Resources**

Historically our operations have generally produced consistent cash flows and required limited capital resources. Short-term borrowings help fund cyclical and seasonality in working capital needs. Long-term debt has been used to fund major acquisitions.

**Summary of Liquidity and Financing Commitments (in millions of dollars)**

|   | As of March 31,<br>2008 | As of December 31,<br>2007 |
|---|-------------------------|----------------------------|
| Cash and cash equivalents                     | \$ 147                  | \$ 181                     |
| Total debt                                    | 695                     | 750                        |
| Shareholders' equity                          | 990                     | 981                        |
| Total capitalization (total debt plus equity) | 1,685                   | 1,731                      |
| Debt to capital ratio                         | 41%                     | 43%                        |

Cash and cash equivalents consisted primarily of marketable securities with maturities at date of acquisition of 90 days or less.

**Table of Contents*****Cash Provided by Operating Activities (in millions of dollars)***

|                              | 2008   | 2007  | Increase |
|------------------------------|--------|-------|----------|
| Three months ended March 31, | \$ 100 | \$ 52 | \$ 48    |

Cash provided by operating activities increased \$48 million mainly from decreased working capital requirements due to the timing of interest, tax and accounts payable payments, and the timing of Jesup's annual planned maintenance shutdown. In 2008, Jesup's maintenance shutdown is scheduled for the second quarter versus the first quarter of 2007.

***Cash Used for Investing Activities (in millions of dollars)***

|                              | 2008    | 2007    | Decrease |
|------------------------------|---------|---------|----------|
| Three months ended March 31, | \$ (38) | \$ (47) | \$ 9     |

Cash used for investing activities decreased \$9 million due to a \$24 million decrease in restricted cash deposits partially offset by \$20 million of timberland purchases in the first quarter of 2008 versus \$9 million of wood chipping facility purchases in the first quarter of 2007.

***Cash Used for Financing Activities (in millions of dollars)***

|                              | 2008    | 2007    | Increase |
|------------------------------|---------|---------|----------|
| Three months ended March 31, | \$ (96) | \$ (17) | \$ (79)  |

Cash used for financing activities increased \$79 million mainly due to higher dividend payments and debt repayment of \$55 million in 2008 compared to a net borrowing of \$12 million in 2007.

***Expected 2008 Expenditures***

There were no pension contributions made during the first quarter of 2008 or 2007; however, we anticipate making discretionary contributions of approximately \$12 million in the next six months. Income tax refunds totaled \$0.3 million in the first quarter of 2008 compared to payments of \$7 million in 2007. We expect 2008 net income tax payments of \$20 million. Capital expenditures are expected to range from \$105 million to \$110 million in 2008. First quarter 2008 spending for environmental costs related to dispositions and discontinued operations was \$1.8 million; full year expenditures of \$8 million are anticipated.

***Liquidity Performance Indicators***

The discussion below is presented to enhance the reader's understanding of our liquidity, ability to generate cash and satisfy rating agency and creditor requirements. This information includes two measures of financial results: Earnings before Interest, Taxes, Depreciation, Depletion and Amortization (EBITDA) and Adjusted Cash Available for Distribution (Adjusted CAD). These measures are not defined by Generally Accepted Accounting Principles (GAAP) and the discussion of EBITDA and Adjusted CAD is not intended to conflict with or change any of the GAAP disclosures discussed above. Management considers these measures to be important to estimate the enterprise and shareholder values of the Company as a whole and of its core segments, and for allocating capital resources. In addition, analysts, investors and creditors use these measures when analyzing our financial condition and cash generating ability. EBITDA is defined by the Securities and Exchange Commission (SEC); however, Adjusted CAD as defined may not be comparable to similarly titled measures reported by other companies.

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EBITDA is a non-GAAP measure of our operating cash generating capacity. For the three months ended March 31, 2008, EBITDA was \$94 million, \$2 million below the prior year period due to lower operating income generated by Timber partially offset by higher Performance Fibers and Real Estate results. Below is a reconciliation of Cash Provided by Operating Activities to EBITDA for the respective periods (in millions of dollars):

|                                       | Three Months Ended<br>March 31, |             |
|---------------------------------------|---------------------------------|-------------|
|                                       | 2008                            | 2007        |
| Cash Provided by Operating Activities | \$ 100.2                        | \$ 52.4     |
| Non-cash cost of real estate sold     | (2.6)                           | (1.4)       |
| Provision for income taxes            | 10.2                            | 7.5         |
| Interest, net                         | 9.7                             | 12.6        |
| Other balance sheet changes           | (23.6)                          | 25.0        |
| <br>EBITDA                            | <br>\$ 93.9                     | <br>\$ 96.1 |

A non-cash expense critical to the economics of our Real Estate business is the non-cash cost of real estate sold. EBITDA plus the non-cash cost of real estate sold for the three months ended March 31, 2008 and 2007 totaled \$97 million and \$98 million, respectively.

Adjusted CAD is a non-GAAP measure of cash generated during a period that is available for dividend distribution, repurchasing our common shares, debt reduction and strategic acquisitions net of associated financing (e.g. realizing like-kind exchange benefits). We define Cash Available for Distribution (CAD) as Cash Provided by Operating Activities less capital expenditures, the tax benefits associated with certain strategic LKE acquisitions, the change in committed cash, the proceeds from matured energy forward contracts and the change in capital expenditures purchased on account. Committed cash represents outstanding checks that have been drawn on our zero balance bank accounts but have not been paid. In compliance with SEC requirements for non-GAAP measures, we also reduce CAD by mandatory debt repayments resulting in the measure entitled Adjusted CAD.

Below is a reconciliation of Cash Provided by Operating Activities to Adjusted CAD (in millions of dollars):

|  | Three Months Ended<br>March 31, |             |
|--|---------------------------------|-------------|
|  | 2008                            | 2007        |
| Cash Provided by Operating Activities        | \$ 100.2                        | \$ 52.4     |
| Capital expenditures                         | (31.8)                          | (31.4)      |
| (Increase)/decrease in committed cash        | (8.0)                           | 27.8 (a)    |
| LKE tax benefits                             | (2.9)                           | (1.0)       |
| Equity-based compensation adjustments        |                                 | 5.8         |
| Other  | 3.9                             | 7.2         |
| <br>Cash Available for Distribution          | <br>61.4                        | <br>60.8    |
| Mandatory debt repayments                    |                                 |             |
| <br>Adjusted Cash Available for Distribution | <br>\$ 61.4                     | <br>\$ 60.8 |

(a) Primarily 2006 interest paid in 2007 and previously reflected as a reduction in 2006 Adjusted CAD.

Adjusted CAD was \$61 million for the three months ended March 31, 2008 and 2007. Higher cash provided by operating activities in 2008 (see above discussion) was offset by an increase in committed cash in 2008. The Adjusted CAD generated in the current period is not necessarily indicative of amounts that may be generated in future periods.

**Liquidity Facilities**



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In October 2007, Rayonier TRS Holdings Inc. ( TRS ) issued \$300 million of 3.75% Senior Exchangeable Notes due 2012. The notes are guaranteed by Rayonier Inc. and are non-callable. The \$300 million in principal will be settled in cash and any excess exchange value will be settled at the option of the Company in either cash or stock of Rayonier Inc. The initial exchange rate is 18.24 shares per \$1,000 principal based on an exchange price equal to 122 percent of the stock s closing price of \$44.93 on

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October 10, 2007, or \$54.81 per share. In separate transactions, TRS and Rayonier Inc., respectively, purchased an exchangeable note hedge and sold warrants which had the effect of increasing the conversion premium from 22 percent to 40 percent, to \$62.90 per share.

We have a \$250 million unsecured revolving credit facility with an accordion feature which allows additional borrowing above \$250 million at market interest rates, in \$25 million increments, up to an aggregate \$100 million, provided no default exists. The facility expires in August 2011. At March 31, 2008, the available borrowing capacity was \$244 million (excluding the accordion feature).

In connection with the Company's installment notes and the \$250 million revolving credit facility, covenants must be met, including ratios based on the facility's definition of EBITDA (Covenant EBITDA). Covenant EBITDA consists of earnings from continuing operations before the cumulative effect of accounting changes and any provision for dispositions, income taxes, interest expense, depreciation, depletion, amortization and the non-cash cost of real estate sold. The Company's dividend restriction covenant limits the sum of dividends in any period of four fiscal quarters to 90 percent of Covenant Funds from Operations (Covenant FFO) plus the aggregate amount of dividends permitted under Covenant FFO in excess of the amount of dividends paid during the prior four fiscal quarters. Covenant FFO is defined as Consolidated Net Income excluding gains or losses from debt restructuring and investments in marketable securities plus depletion, depreciation, amortization and the non-cash cost of real estate sold. Under a covenant relating to the \$328 million of installment notes, Rayonier Forest Resources, L.P. (RFR), a wholly-owned REIT subsidiary, may not incur additional debt unless, at the time of incurrence, and after giving pro forma effect to the receipt and application of the proceeds of such debt, RFR meets or exceeds a minimum ratio of cash flow to fixed charges. RFR's ability to make certain quarterly distributions to Rayonier Inc. is limited to an amount equal to RFR's available cash, which consists of its opening cash balance plus proceeds from permitted borrowings. At March 31, 2008, the Company is in compliance with all material covenants.

The covenants listed below, which are the most significant financial covenants in effect as of March 31, 2008, are calculated on a trailing 12-month basis:

|  | <b>Covenant Requirement</b> | <b>Actual ratio at March 31, 2008</b> | <b>Favorable (Unfavorable)</b> |
|--|-----------------------------|---------------------------------------|--------------------------------|
| Covenant EBITDA to consolidated interest expense should not be less than               | 2.50 to 1                   | 7.93                                  | 5.43                           |
| Total debt to Covenant EBITDA should not exceed  | 4.00 to 1                   | 1.63                                  | 2.37                           |
| RFR cash flow available for fixed charges to RFR fixed charges should not be less than | 2.50 to 1                   | 4.94                                  | 2.44                           |
| Dividends paid should not exceed 90 percent of Covenant FFO                            | 90%                         | 44%                                   | 46%                            |

In addition to the financial covenants listed above, the installment notes, Senior Exchangeable Notes and credit facility include customary covenants that limit the incurrence of debt, the disposition of assets, and the making of certain payments between RFR and Rayonier among others. An asset sales covenant in the RFR installment note-related agreements requires us, subject to certain exceptions, to either reinvest cumulative timberland sales proceeds in excess of \$100 million (the excess proceeds) in timberland-related investments or, once the amount of excess proceeds not reinvested exceeds \$50 million, to offer the note holders prepayment of the notes ratably in the amount of the excess proceeds. As of March 31, 2008 and December 31, 2007, there were no excess proceeds.

**Contractual Financial Obligations and Off-Balance Sheet Arrangements**

The following updates the Contractual Financial Obligations table as presented on page 38 of our 2007 Annual Report on Form 10-K.

In the first quarter of 2008, the Company finalized a consent decree with the Environmental Protection Division of the Georgia Department of Natural Resources (EPD) that resolves certain issues relating to the color of the Jesup mill's permitted effluent discharged to the Altamaha River. These projects will be completed over a seven year period pursuant to a timeframe set forth in the decree at a cost of approximately \$75 million.

No material changes to guarantees or financial instruments such as letters of credit and surety bonds occurred during the first three months of 2008. See Note 9 *Guarantees*, for details on the letters of credit, surety bonds and total guarantees outstanding as of March 31, 2008.

**Table of Contents****Segment EBITDA**

EBITDA is also used for evaluating segment cash return on investment, allocating resources and for valuation purposes. EBITDA by segment is a critical valuation measure used by the Chief Operating Decision Maker, existing shareholders and potential shareholders to measure how management is performing relative to the assets with which they have been entrusted. EBITDA by segment for the three months ended March 31, 2008 and 2007 was as follows (millions of dollars):

|                     | <b>Three Months Ended<br/>March 31,</b> |                |
|---------------------|---|----------------|
|                     | <b>2008</b>                             | <b>2007</b>    |
| <b>EBITDA</b>       |   |                |
| Timber              | \$ 30.1                                 | \$ 48.0        |
| Real Estate         | 24.4                                    | 17.4           |
| Performance Fibers  | 48.2                                    | 42.4           |
| Wood Products       | (1.1)                                   | (1.7)          |
| Other Operations    | (0.6)                                   | (1.3)          |
| Corporate and other | (7.1)                                   | (8.7)          |
| <b>Total</b>        | <b>\$ 93.9</b>                          | <b>\$ 96.1</b> |

The following tables reconcile Cash Provided by Operating Activities by segment to EBITDA by segment (millions of dollars):

|  | <b>Timber</b>  | <b>Real<br/>Estate</b> | <b>Performance<br/>Fibers</b> | <b>Wood<br/>Products</b> | <b>Other<br/>Operations</b> | <b>Corporate<br/>and other</b> | <b>Total</b>   |
|--|----------------|------------------------|-------------------------------|--------------------------|-----------------------------|--------------------------------|----------------|
| <b>Three Months Ended March 31, 2008</b> |                |                        |                               |                          |                             |                                |                |
| Cash Provided by Operating Activities    | \$ 26.5        | \$ 26.2                | \$ 58.3                       | \$ (4.0)                 | \$ 2.2                      | \$ (9.0)                       | \$ 100.2       |
| Less: Non-cash cost of real estate sold  |                | (2.6)                  |                               |                          |                             |                                | (2.6)          |
| Add: Provision for income taxes          |                |                        |                               |                          |                             | 10.2                           | 10.2           |
| Interest, net                            |                |                        |                               |                          |                             | 9.7                            | 9.7            |
| Other balance sheet changes              | 3.6            | 0.8                    | (10.1)                        | 2.9                      | (2.8)                       | (18.0)                         | (23.6)         |
| <b>EBITDA</b>                            | <b>\$ 30.1</b> | <b>\$ 24.4</b>         | <b>\$ 48.2</b>                | <b>\$ (1.1)</b>          | <b>\$ (0.6)</b>             | <b>\$ (7.1)</b>                | <b>\$ 93.9</b> |
| <b>Three Months Ended March 31, 2007</b> |                |                        |                               |                          |                             |                                |                |
| Cash Provided by Operating Activities    | \$ 47.3        | \$ 19.0                | \$ 45.4                       | \$ (1.3)                 | \$ (7.3)                    | \$ (50.7)                      | \$ 52.4        |
| Less: Non-cash cost of real estate sold  |                | (1.4)                  |                               |                          |                             |                                | (1.4)          |
| Add: Provision for income taxes          |                |                        |                               |                          |                             | 7.5                            | 7.5            |
| Interest, net                            |                |                        |                               |                          |                             | 12.6                           | 12.6           |
| Other balance sheet changes              | 0.7            | (0.2)                  | (3.0)                         | (0.4)                    | 6.0                         | 21.9                           | 25.0           |
| <b>EBITDA</b>                            | <b>\$ 48.0</b> | <b>\$ 17.4</b>         | <b>\$ 42.4</b>                | <b>\$ (1.7)</b>          | <b>\$ (1.3)</b>             | <b>\$ (8.7)</b>                | <b>\$ 96.1</b> |

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The following table provides sales volumes by segment:

|  | <b>Three Months Ended<br/>March 31,</b> |              |
|--|---|--------------|
|  | <b>2008</b>                             | <b>2007</b>  |
| <b>Timber</b>                                      |   |              |
| Western region, in millions of board feet          | 59                                      | 79           |
| Eastern region, in thousands of short green tons   | 1,312                                   | 1,643        |
| <b>Real Estate</b>                                 |   |              |
| Acres sold   |   |              |
| Development  | 47                                      | 123          |
| Rural  | 6,488                                   | 6,015        |
| Non-strategic timberlands                          | 4,073                                   |              |
| <b>Total</b>                                       | <b>10,608</b>                           | <b>6,138</b> |
| <b>Performance Fibers</b>                          |   |              |
| Sales Volume                                       |   |              |
| Cellulose specialties, in thousands of metric tons | 107                                     | 114          |
| Absorbent materials, in thousands of metric tons   | 56                                      | 55           |
| Production as a percent of capacity                | 94.7%                                   | 95.1%        |
| <b>Lumber</b>                                      |   |              |
| Sales volume, in millions of board feet            | 74                                      | 73           |

The following table provides timber sales and operating income by geographic location (millions of dollars):

|                  | <b>Three Months Ended</b> |                           |
|------------------|---------------------------|---------------------------|
|                  | <b>March 31,<br/>2008</b> | <b>March 31,<br/>2007</b> |
| <b>Timber</b>    |                           |                           |
| Sales            |                           |                           |
| Western          | \$ 20.6                   | \$ 30.7                   |
| Eastern          | 24.1                      | 31.1                      |
| New Zealand      | 2.5                       | 3.2                       |
| <b>Total</b>     | <b>\$ 47.2</b>            | <b>\$ 65.0</b>            |
| Operating income |                           |                           |
| Western          | \$ 8.5                    | \$ 18.0                   |
| Eastern          | 2.5                       | 7.8                       |
| New Zealand      | 1.0                       | 0.5                       |
| <b>Total</b>     | <b>\$ 12.0</b>            | <b>\$ 26.3</b>            |

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**  
**Market Risk**

We are exposed to various market risks, including changes in interest rates, commodity prices and foreign exchange rates. Our objective is to minimize the economic impact of these market risks. We use derivatives in accordance with policies and procedures approved by the Finance Committee of the Board of Directors. Derivatives are managed by a senior executive committee whose responsibilities include initiating, managing and monitoring resulting exposures. We do not enter into financial instruments for trading or speculative purposes.



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Cyclical pricing of commodity market paper pulp is one of the factors that influence Performance Fibers prices, particularly in the absorbent materials product line. However, since we are a non-integrated producer of specialized performance fibers for non-papermaking end uses, our high-value product mix tends to lag (on both the upturn and downturn) commodity paper pulp prices with pricing adjustments that are less severe. The risk is mitigated somewhat by the terms of our cellulose specialty contracts which are effective into 2011 and represent nearly all of our high-value cellulose specialties production.

We periodically enter into interest rate swap agreements to manage exposure to interest rate changes. These swaps involve the exchange of fixed and variable interest rate payments without exchanging principal amounts. At March 31, 2008, we had no interest rate swap agreements.

The fair market value of our long-term fixed interest rate debt is subject to interest rate risk; however, we intend to hold most of our debt until maturity. Generally, the fair market value of fixed-interest rate debt will increase as interest rates fall and will decrease as interest rates rise.

We periodically enter into commodity forward contracts to fix some of our fuel oil and natural gas costs. The forward contracts partially mitigate the risk of a change in Performance Fibers margins resulting from an increase or decrease in these energy costs. A hypothetical 10 percent increase/decrease in the prevailing market price of fuel oil hedged at March 31, 2008 would result in a change of \$0.4 million in our pre-tax income. We do not enter into commodity forwards for trading or speculative purposes. The net amounts paid or received under the contracts are recognized as an adjustment to fuel oil or natural gas expense. Our natural gas and fuel oil contracts do not qualify for hedge accounting and as such, mark-to-market adjustments are recorded in Other operating income, net. See Note 8 *Financial Instruments* for outstanding forward contracts at March 31, 2008 as well as gains and losses recognized from such contracts.

Primarily all of our revenues and expenses are U.S. dollar-denominated. However, the JV is subject to the risks of foreign currency fluctuations (See Note 6 *Joint Venture Investment* for additional information on the JV). At March 31, 2008, there were no outstanding forward foreign currency contracts to purchase New Zealand dollars.

For a full description of our market risk, please refer to Item 7, *Management Discussion and Analysis of Financial Condition and Results of Operations*, in the 2007 Annual Report on Form 10-K.

**Item 4. Controls and Procedures**

Rayonier management is responsible for establishing and maintaining adequate disclosure controls and procedures. Disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the Exchange Act)), are designed with the objective of ensuring that information required to be disclosed by the Company in reports filed under the Exchange Act, such as this quarterly report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

Because of the inherent limitations in all control systems, no control evaluation can provide absolute assurance that all control exceptions and instances of fraud have been prevented or detected on a timely basis. Even systems determined to be effective can provide only reasonable assurance that their objectives are achieved.

Based on an evaluation of our disclosure controls and procedures as of the end of the period covered by this quarterly report on Form 10-Q, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that the design and operation of the disclosure controls and procedures were effective as of March 31, 2008.

In the quarter ended March 31, 2008, based upon the evaluation required by paragraph (d) of SEC Rules 13a-15 and 15d-15, there were no changes in our internal controls over financial reporting that would materially affect or are reasonably likely to materially affect our internal control over financial reporting.

**Table of Contents****PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

See Notes 10 and 11 of the Notes to Condensed Consolidated Financial Statements set forth in Part I of this Report, which are hereby incorporated by reference.

**Item 1A. Risk Factors**

There were no material changes from the risk factors previously disclosed in our Form 10-K for the year ended December 31, 2007. For a full description of these risk factors, please refer to Item 1A *Risk Factors*, in the 2007 Annual Report on Form 10-K.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

In 1996, we began a Common Share repurchase program to minimize the dilutive effect on earnings per share of our employee incentive stock plans. This program limits the number of shares that may be purchased each year to the greater of 1.5 percent of outstanding shares at the beginning of the year or the number of incentive shares issued to employees during the year. In October 2000 and July 2003, our Board of Directors authorized the purchase of additional shares totaling 1.4 million. These shares were authorized separately from the 1.5 percent of outstanding shares anti-dilutive program, neither of which have expiration dates.

The following table provides information regarding our purchases of Rayonier common stock during the first quarter ended March 31, 2008:

| Period                                | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs |
|---------------------------------------|----------------------------------|------------------------------|--|--|
| January 1, 2008 to January 31, 2008   | 74,230 *                         | \$ 44.29                     |  |  |
| February 1, 2008 to February 29, 2008 |                                  |                              |  |  |
| March 1, 2008 to March 31, 2008       | 5,000                            | 39.94                        | 5,000  | 2,471,089  |
| Total                                 | 79,230                           |                              | 5,000  | 2,471,089  |

\* Repurchased to satisfy the minimum tax withholding requirements related to the vesting of performance shares and restricted shares under the 2004 Rayonier Incentive Stock Plan.

**Item 3. Defaults Upon Senior Securities**

Not applicable.

**Item 4. Submission of Matters to a Vote of Security Holders**

No matter was submitted to a vote of security holders of Rayonier during the first quarter of 2008.

**Item 5. Other Information**  
Not applicable.



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**Item 6. Exhibits**

|      |  |                    |
|------|--|--------------------|
| 31.1 | Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act     | Filed herewith     |
| 31.2 | Certification of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act | Filed herewith     |
| 32   | Certification pursuant to Section 906 of the Sarbanes-Oxley Act                                    | Furnished herewith |

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**SIGNATURE**

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

RAYONIER INC.

By: /s/ HANS E. VANDEN NOORT  
Hans E. Vanden Noort  
*Senior Vice President and Chief Financial Officer*

April 24, 2008