

Potlatch

POTLATCH CORPORATION -- SIX MONTHS REPORT, JUNE 30, 2004 HIGHLIGHTS

Unaudited (Dollars in thousands - except per-share amounts)

	Quarter Ended		Six Months Ended	
	June 30		June 30	
	2004	2003	2004	2003
Net sales	\$ 472,639	\$ 368,094	\$ 893,061	\$ 702,896
Earnings (loss) from continuing operations	49,568	6,822	71,386	(2,069)
Net earnings (loss)	49,568	6,649	71,386	(2,916)
Net earnings (loss) per common share from continuing operations:				
Basic	\$ 1.68	\$.24	\$ 2.43	\$ (.07)
Diluted	1.68	.24	2.42	(.07)
Net earnings (loss) per common share:				
Basic	1.68	.23	2.43	(.10)
Diluted	1.68	.23	2.42	(.10)
Dividends per common share (annual rate)	.60	.60	.60	.60

This report contains, in addition to historical information, certain forward-looking statements. These forward-looking statements are based on management's best estimates and assumptions regarding future events, and are therefore subject to known and unknown risks and uncertainties and are not guarantees of future performance. The company's actual results could differ materially from those expressed or implied by forward-looking statements. The company disclaims any intent or obligation to update these forward-looking statements.

Potlatch Corporation reported significantly higher earnings for the second quarter of 2004, compared to the second quarter of 2003, due primarily to continued strength in its wood products markets.

Improved financial performance from the company's Pulp and Paperboard and Consumer Products operating segments also contributed to the positive results, while the Resource segment posted lower earnings compared to the prior year second quarter. Second quarter 2003 earnings were positively affected by significant interest income of \$12.5 million from a federal income tax settlement.

For the second quarter of 2004, the company reported net earnings of \$49.6 million, or \$1.68 per diluted common share, compared to earnings from continuing operations of \$6.8 million, or \$.24 per diluted common share for the same period in 2003. Including discontinued operations, the company earned \$6.6 million or \$.23 per diluted common share for the second quarter of 2003. Net sales for the second quarter of 2004 were \$472.6 million, substantially higher than the \$368.1 million recorded in the second quarter of 2003.

Net earnings for the first half of 2004 totaled \$71.4 million or \$2.42 per diluted common share. The loss from continuing operations for the first half of 2003 was \$2.1 million or \$.07 per diluted common share. Including discontinued operations, the net loss for the first half of 2003 totaled \$2.9 million or \$.10 per diluted common share. Net sales for the first half of 2004 were \$893.1 million, compared with \$702.9 million for 2003's first half.

The Resource segment reported operating income of \$6.8 million for the second quarter of 2004, substantially lower than the \$23.5 million earned in the second quarter of 2003. Land sales revenue totaled \$1.1 million in the second quarter of 2004, versus \$14.1 million in the second quarter of 2003. The June 2003 sale of approximately 15,300 acres of hardwood timberland in Arkansas was the primary reason for the unfavorable comparison. Lower fiber sales in Arkansas during the second quarter of 2004 also negatively affected earnings.

Operating income for the Wood Products segment was \$94.4 million for the second quarter of 2004, a dramatic increase over the \$2.3 million earned in the second quarter of 2003. The conditions that started the rally in wood

products markets during the third quarter of 2003 – low interest rates, a strong housing market and a weaker U.S. dollar – have continued through the second quarter of 2004. Selling prices for all of the segment's products were higher when compared to the second quarter of 2003, especially oriented strand board, which was more than double last year's price early in the quarter. Prices began an expected decline mid-quarter, but still remained at favorable levels at the end of 2004's second quarter. The higher selling prices more than made up for lower shipments of oriented strand board, lumber and particleboard on a quarter-to-quarter comparison.

The Pulp and Paperboard segment reported operating income for the second quarter of \$5.9 million, versus a loss of \$1.2 million for 2003's second quarter. The segment benefited from higher paperboard and pulp shipments compared to 2003's second quarter, as well as higher selling prices for pulp. Additionally, higher production at both of the segment's facilities, especially the mill in Lewiston, Idaho, resulted in lower per ton costs. Pulp prices have steadily improved during the first half of 2004, and paperboard prices have improved modestly in recent months.

The Consumer Products segment incurred an operating loss of \$1.2 million during the quarter, smaller than the operating loss of \$5.0 million posted in the second quarter of 2003. Although markets for consumer tissue products continued to be very competitive, segment shipments increased 18% over the second quarter of 2003, and net selling prices also showed a slight improvement. Both shipment and selling price measures were positively affected by the rollout of the ultra towel product manufactured at the company's new Las Vegas tissue facility. Results for the second quarter of 2003 were adversely affected by downtime taken on numerous converting lines to reduce finished goods inventory levels.



L. Pendleton Siegel
Chairman and Chief Executive Officer
July 19, 2004

Statements of Operations and Comprehensive Income

Unaudited (Dollars in thousands - except per-share amounts)

	Quarter Ended		Six Months Ended	
	June 30		June 30	
	2004	2003	2004	2003
Net sales	\$ 472,639	\$ 368,094	\$ 893,061	\$ 702,896
Costs and expenses:				
Depreciation, amortization and cost of fee timber harvested	25,041	25,202	52,124	52,061
Materials, labor and other operating expenses	330,449	311,915	652,554	604,259
Selling, general and administrative expenses	23,022	20,239	45,477	37,491
Restructuring charges	(87)	-	1,193	227
	378,425	357,356	751,348	694,038
Earnings from operations	94,214	10,738	141,713	8,858
Interest expense	(12,478)	(12,128)	(24,338)	(24,890)
Interest income	491	12,573	619	12,640
Earnings (loss) before taxes	82,227	11,183	117,994	(3,392)
Provision (benefit) for taxes	32,659	4,361	46,608	(1,323)
Earnings (loss) from continuing operations	49,568	6,822	71,386	(2,069)
Discontinued operations:				
Loss from discontinued operations (including loss on disposal of \$-, \$-, \$- and \$45)	-	(283)	-	(1,389)
Income tax benefit	-	(110)	-	(542)
Net earnings (loss)	49,568	6,649	71,386	(2,916)
Other comprehensive loss, net of tax:				
Cash flow hedges:				
Net derivative losses, net of income tax benefit of \$-, \$-, \$44 and \$-	-	-	(68)	-
Comprehensive income (loss)	\$ 49,568	\$ 6,649	\$ 71,318	\$ (2,916)
Net earnings (loss) per common share from continuing operations:				
Basic	\$ 1.68	\$.24	\$ 2.43	\$ (.07)
Diluted	1.68	.24	2.42	(.07)
Net earnings (loss) per common share:				
Basic	1.68	.23	2.43	(.10)
Diluted	1.68	.23	2.42	(.10)
Average shares outstanding (in thousands):				
Basic	29,498	28,679	29,372	28,648
Diluted	29,611	28,679	29,487	28,648

Certain 2003 amounts have reclassified to conform to the 2004 presentation.

Condensed Balance Sheets

2004 amounts unaudited (Dollars in thousands - except per-share amounts)

	June 30,	December 31,
	2004	2003
Assets		
Current assets:		
Cash and short-term investments	\$ 204,606	\$ 47,281
Receivables, net	123,027	105,345
Inventories	138,219	159,678
Prepaid expenses	20,511	18,315
Total current assets	486,363	330,619
Land other than timberlands	9,325	8,831
Plant and equipment, at cost		
less accumulated depreciation	718,212	740,342
Timber, timberlands and related logging facilities	401,936	398,899
Other assets	119,479	118,686
	\$ 1,735,315	\$ 1,597,377
Liabilities and Stockholders' Equity		
Current liabilities:		
Current installments on long-term debt	\$ 1,106	\$ 507
Accounts payable and accrued liabilities	171,127	169,310
Total current liabilities	172,233	169,817
Long-term debt	617,194	618,278
Other long-term obligations	271,999	266,514
Deferred taxes	118,331	71,917
Stockholders' equity	555,558	470,851
	\$ 1,735,315	\$ 1,597,377
Stockholders' equity per common share	\$ 18.82	\$ 16.33
Working capital	\$ 314,130	\$ 160,802
Current ratio	2.8:1	1.9:1

Condensed Statements of Cash Flows

Unaudited (Dollars in thousands)

	Six Months Ended June 30	
	2004	2003
CASH FLOWS FROM OPERATIONS		
Net earnings (loss)	\$ 71,386	\$ (2,916)
Adjustments to reconcile net earnings (loss) to net operating cash flows:		
Loss from discontinued operations	-	820
Loss on disposal of discontinued operations	-	60
Depreciation, amortization and cost of fee timber harvested	52,124	52,061
Deferred taxes	46,414	(1,865)
Working capital changes	13,418	21,072
Other, net	428	-
Net cash provided by operating activities of continuing operations	183,770	69,232
CASH FLOWS FROM INVESTING		
Decrease in restricted cash	-	15,069
Increase in short-term investments	(154,534)	(24,924)
Additions to plant and properties	(25,475)	(29,450)
Other, net	(4,935)	(4,804)
Net cash used for investing activities of continuing operations	(184,944)	(44,109)
CASH FLOWS FROM FINANCING		
Change in book overdrafts	(10,019)	757
Decrease in notes payable	-	(5,000)
Retirement of long-term debt	(485)	(16,385)
Issuance of treasury stock	21,737	2,747
Dividends	(8,777)	(8,592)
Other, net	1,509	4,841
Net cash provided by (used for) financing activities of continuing operations	3,965	(21,632)
Cash from continuing operations	2,791	3,491
Cash from discontinued operations	-	3,608
Increase in cash	2,791	7,099
Cash at beginning of period	7,190	8,973
Cash at end of period	\$ 9,981	\$ 16,072

Segment Information

(Dollars in thousands)

	Quarter Ended June 30		Six Months Ended June 30	
	2004	2003	2004	2003
Net Sales				
Resource	\$ 44,784	\$ 61,829	\$ 106,574	\$ 106,800
Wood products				
Oriented strand board	129,394	62,410	233,287	114,643
Lumber	94,268	74,068	171,927	137,719
Plywood	16,099	9,808	31,617	19,117
Particleboard	5,244	3,901	10,089	7,196
Other	6,701	6,716	13,840	15,303
Total wood products net sales	251,706	156,903	460,760	293,978
Pulp and paperboard				
Paperboard	119,864	115,300	228,393	220,221
Pulp	18,160	13,382	30,541	26,522
Total pulp and paperboard net sales	138,024	128,682	258,934	246,743
Consumer products	83,145	67,414	157,113	145,478
	517,659	414,828	983,381	792,999
Intersegment sales	(45,020)	(46,734)	(90,320)	(90,103)
Total net sales	\$ 472,639	\$ 368,094	\$ 893,061	\$ 702,896
	Quarter Ended June 30		Six Months Ended June 30	
	2004	2003	2004	2003
Operating income (loss)				
Resource	\$ 6,756	\$ 23,534	\$ 18,809	\$ 34,655
Wood products	94,447	2,343	152,246	(1,268)
Pulp and paperboard	5,872	(1,159)	(1,889)	(10,492)
Consumer products	(1,238)	(4,974)	(5,055)	1,828
Eliminations	1,669	(1,400)	2,104	(1,330)
	107,506	18,344	166,215	23,393
Corporate	(25,279)	(7,161)	(48,221)	(26,785)
Earnings (loss) from continuing operations before taxes	\$ 82,227	\$ 11,183	\$ 117,994	\$ (3,392)



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Sales Price/Unit				
	Quarter Ended		Six Months Ended	
	June 30		June 30	
	2004	2003	2004	2003
Wood products (\$ per unit)				
Oriented strand board (m. sq. ft., 3/8" basis)	\$ 381	\$ 181	\$ 351	\$ 172
Lumber (m. bd. ft.)	465	345	431	343
Plywood (m. sq. ft., 3/8" basis)	395	281	380	278
Particleboard (m. sq. ft., 3/4" basis)	297	208	282	204
Pulp and paperboard (\$ per ton)				
Paperboard	640	638	635	644
Pulp	496	361	459	375
Consumer products (\$ per ton)				
Tissue	1,823	1,749	1,804	1,800

Shipment Information				
	Quarter Ended		Six Months Ended	
	June 30		June 30	
	2004	2003	2004	2003
Wood products				
Oriented strand board (m. sq. ft., 3/8" basis)	339,271	344,290	663,885	666,983
Lumber (m. bd. ft.)	202,863	214,542	398,880	401,209
Plywood (m. sq. ft., 3/8" basis)	40,766	34,863	83,138	68,670
Particleboard (m. sq. ft., 3/4" basis)	17,633	18,784	35,811	35,257
Pulp and paperboard				
Paperboard (tons)	187,340	180,806	359,589	342,163
Pulp (tons)*	9,627	6,505	18,345	18,662
Consumer products				
Tissue (tons)	45,599	38,537	87,068	80,793

* Excludes pulp used internally.