Implications of Changing Ownership in the Australian Forestry Sector

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About New Forests

- Forestry investment management business for institutional investors—superannuation funds, pension funds, insurance companies, endowments
- Currently managing $1 billion in forestry assets
- Head office in Sydney, 29 staff in Australia, New Zealand, Singapore, and USA
- Managing 325,000 hectares of land and forestry assets across Australia
Why are Institutional Investors Interested in Owning Forestry Assets?

- After global financial crisis, increasing demand for ‘real assets’ such as real estate, infrastructure and forestry
- Forestry is seen as having relatively stable returns via either capital appreciation (eg growth) or income (eg timber sales)
- Forestry returns have been positively correlation with inflation but with low or negative correlation to other key assets (listed equities, bonds)
What Attracts Institutional Investors to Australian forestry?

- A stable business environment with a strong economy, good infrastructure, skilled labour, technical expertise, defensible property rights, and attractive tax and commercial environment
- A high quality pool of existing hardwood and softwood assets
- A strong domestic market for softwood timber

*These translate into a cost of capital for Australian forestry which is close to the USA and 500 to 600 bp better than Latin America or Asia*
<table>
<thead>
<tr>
<th>Country</th>
<th>Investible Assets*</th>
<th>Discount Rates (real IRR, pre-tax)</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA/Canada</td>
<td>$70-80 billion</td>
<td>6-6.5%</td>
</tr>
<tr>
<td>New Zealand</td>
<td>$7-8 billion</td>
<td>8-9%</td>
</tr>
<tr>
<td>Australia</td>
<td>$6 billion</td>
<td>7-8%</td>
</tr>
<tr>
<td>Brazil/Uruguay/Chile</td>
<td>$25 billion</td>
<td>8-14%</td>
</tr>
<tr>
<td>Asia/Africa</td>
<td>$5 billion</td>
<td>10-18%</td>
</tr>
</tbody>
</table>

*source HNRG, New Forests estimates
Investible Universe of Australian Forestry Assets

- Australia has about 1 million hectares of softwood plantation and 1 million hectares of hardwood plantation
- Estimated value of softwood forests is $3.5 billion and hardwood forests $2.5 billion
- Institutional investment to date is about $1.5 billion in softwood, and $1 billion in hardwood
- We expect to see most remaining plantations evolve into institutional ownership in the next 2-4 years
What will a Forestry Sector under Institutional Ownership look like?

- Assets will be owned in various unlisted corporate and trust structures
- Three or four professional investment managers will control most assets
- Assets will become tightly held and turn over rarely once the State Governments have exited and MIS has been rationalized
- Forest management will be via a mix of ‘in-house’ and outsourced approaches
- Strong emphasis on commercial returns, sustainability and risk reduction
Evolution of Softwood Estate

- Australia has a domestically focussed softwood plantation sector, serving the domestic housing industry.
- Domestic markets are less volatile than export markets, and cost of capital is slightly lower for these assets vs New Zealand radiata plantations.
- General view is that Australian radiata pine plantation estate is a world class asset.
- Need for further investment in plantation expansion and processing facilities—some hardwood plantations may be shifted to softwood next rotation.
Evolution of Hardwood Estate

- Likely consolidation into Western Australia (Albany/Bunbury), Green Triangle, and N. Tasmania
- 200,000 to 300,000 ha will likely go back to agriculture
- Economic margin will be affected by carbon rules, timber pricing, Australian dollar, etc. FOB Prices are about 20% off the peak, which translates into 50% drop in stumpage value
- Market is evolving from bi-lateral relationship with Japanese paper industry to mix of Japanese and Chinese markets, including emerging peeler log market
- Question about whether bio-energy or biomaterials will become significant demand in coming years
Some General Thoughts

- Australia is today seen as a key part of a global forestry investment portfolio
- There is substantial capital available for forestry investment from institutional investors, but must meet risk-adjusted return expectations
- With the ending of the MIS era, and reducing role of state governments, the forestry sector will need to be internationally competitive, focussed on productivity and able to compete for land with agriculture—this will determine how much timber is grown in Australia vs imported
- Government interventions should support investment and productivity enhancement