

OLSEN NEWS



PF Olsen and Company
Professional Forestry Services **Ltd**

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▲ *Carbon Sinks Update*

The industry is continuing to engage with Climate Change Minister Pete Hodgson's officials in respect of initiatives that would see the forest industry benefit from the windfall gain the Government has awarded itself by effectively nationalizing the post-1990 forest sink credits. Negotiations are at a critical stage. Determinants of success for industry will be:

- Government commitments to projects that can help the industry achieve its Vision in 2025.
- The level of Government financial support for those initiatives.
- A fair deal for the owners of post-1990 forests planted on new land.

The industry is seeking significant financial support for some "big-ticket" projects that are well beyond the capacity of industry to fund alone under our present methods of raising funds for pan-industry projects. The projects are closely aligned with the objectives of the Wood Processing Strategy. Progress is positive and the relationship between industry and government officials is constructive but it remains unclear whether a satisfactory outcome for the post-1990 forest owners will be reached.

Of course one immediate outcome we can expect if the post-1990 forest owners are not dealt with fairly is a virtual halt to all new land planting from already low levels, and some harvested forest land reverting to pasture. That outcome has serious consequences to New Zealand's carbon balances in the future, as the forestry sector would itself become a net emitter of

carbon from about 2016. It is difficult to see how the Government expects to continue to meet its Kyoto commitments, as well as a growing economy, without some form of encouragement for new planting in the short term.

In the longer term, the only sustainable incentive for continued planting will be increased stumpages. That in turn can be achieved if we get massive new investment into wood processing in New Zealand. To do that NZ must be internationally competitive as a place to invest. The government must urgently address some blockages to investment, the most obvious being:

- Shortage of energy supply and high costs when insufficient hydropower is available.
- RMA delays and costs.
- Trade access (tariff and non-tariff barriers for processed wood products).

We will keep you informed on these issues and initiatives.

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▲ *WQI Limited*

WQI Ltd is a newly formed company set up to research wood quality issues affecting the marketing and profitability of our radiata pine industry. The company is not a research organization – it is in the business of funding, directing, commercialising and implementing research for the benefit of its shareholders. The research is to be contracted primarily to Forest Research, University of Canterbury, CSIRO (Australia's leading research provider) and Industrial Research Ltd.

The research has been split into four key objectives aimed at understanding the fundamental determinants of wood quality, and developing tools that allow segregation of logs, flitch or sawn timber as early as possible in the processing value chain. The aim is to reduce waste and costs by only sending logs and timber that will meet final product specifications through each processing line, and to deliver to customers only final products that perform as expected.

Dr Keith Mackie, formerly Chief Scientist at Forest Research (FR), has been appointed CEO, and the only employee of WQI Ltd, in a rigorous selection process. In his former roles at FR and in the set-up process for WQI Ltd, Dr Mackie has built up an excellent relationship with scientists, industry and the Foundation for Research Science and Technology (FRST). WQI Ltd has most of the larger forest owning companies as shareholders, as well as key research providers. It has an initial budget of nearly \$2.0 million/annum, funded 50:50 by the shareholders and FRST. Olsens are a shareholder in WQI Ltd and CEO Peter Clark is a Director of the company.

▲ *Harvesting & Marketing*

In January of this year, Peter Weblin took up the position of Olsens Harvesting and Marketing Manager. He is based in Rotorua.

Peter has had 20 years experience in the New Zealand forestry industry. This has included

roles with Fletcher Challenge Forests, Rayonier and Works Infrastructure Forestry Services.

Whilst having a general forest management background, Peter has focused on the areas of timber yield management, harvest scheduling and timber sales management and marketing.

Peter notes that as we head into winter, softening prices for timber and the strike at the Kinleith pulp mill do little to support harvesting and marketing. While forests and woodlots continue to mature, owners in the Central North Island are reluctant to initiate harvesting because of low prices and high pulp log stocks.



Peter Weblin

Export log demand has been steady but NZ\$ at-wharf-gate prices have been eroded by the high NZ\$/US\$ exchange rate and high ocean freight costs. The once promising US market is awash with low-cost pine from South America and even a strong property sector is not enough to prevent significant price erosion. The New Zealand and Australian construction sectors, on the other hand, have been buoyant and have provided the market with some strength. Indicators, however, are now pointing towards a slowdown in these market segments as well.

On a more positive note, forestry as an asset class is attracting renewed attention. With returns from equity and bond markets being re-rated downwards and property looking fully priced in many markets, traditional forestry returns are looking increasingly attractive. And

of course, one of the great advantages of forestry is the relatively wide harvesting window. Whilst the economic rotation age of radiata pine may be described as a single year, say 25 years, there is very little value lost if harvesting is delayed some four or five years. "The woodlot continues to increase in value as it grows", says Peter Weblin, "and only marginally below the cost of capital".

Despite the current market situation, Olsens have continued to be successful in winning new work under competitive tender. Recently we secured the harvesting and marketing services for 20,000 tonnes of radiata pine in the Far North.

Even though timber markets are currently soft, there are some important steps that owners of nearly mature woodlots should take in order to ensure the best possible returns from their investment.

This time last year timber markets were relatively strong, but it was difficult to find suitable contractors. Today we face the opposite situation. This situation is likely to reverse again in the future and if the market demand swings strongly upward many woodlot owners could be on a long waiting list for logging contractors.

The most important steps an owner of a nearly mature woodlot can take is to become Harvest-ready. Being Harvest-ready means:

- Having taken time to carefully plan and initiate road access.
- Developed a harvest plan.
- Applying for a Resource Consent including consultation where required.
- Undertaking a timber inventory to identify the best market channels for marketing the timber.
- Scheduling a logging contractor for the harvest operations.

To encourage woodlot owners to take the steps to become harvest-ready, Olsens is offering a special service. In most cases, Olsens will undertake the harvesting and marketing services and hold the costs until the commencement of

harvesting. This means woodlot owners are not out of pocket and expenses are matched to the period when timber sales revenues are received.

Once harvest-ready we will also keep a close eye on timber markets and communicate developments to the woodlot owner. When a decision is made to commence harvesting there is minimal delay and the prospect of engaging an appropriate logging contractor is enhanced. As usual, Olsens offer a fully independent harvesting and marketing service, ensuring access to the market segments offering you the best possible returns for your timber. If you would like to find out more about our Harvesting and Marketing services please contact Peter Weblin.

▲ *Log Markets*

General

The climb up the face of the "wave of opportunity" continues. The 2002 annual log harvest of 22.6 million m³ was 9.2% larger than that of 2001.

Meanwhile wood growers face a difficult patch. The NZ\$ log prices fell sharply at the end of 2002, while harvest costs rose by some 20%. Most of the pressure for higher costs followed the re-negotiation of key supplier harvest contracts by the large forestry companies.

Export Log Markets

Demand for logs remains buoyant with some small increases reported in the US\$ price paid at the ports of discharge. These gains are more than offset by the rise of the exchange rate of the NZ\$ relative to US\$, plus increases in ocean freight costs of about US\$9/tonne.

China continued to expand its log purchases from New Zealand over the past year, but this growth may be slowed by the impact of the SARS epidemic.

The current NZ\$ wharf gate prices obtained for the lowest quality export logs such as the KI and KIS (pulp) are at a level where the net return from these logs grades may be negative.

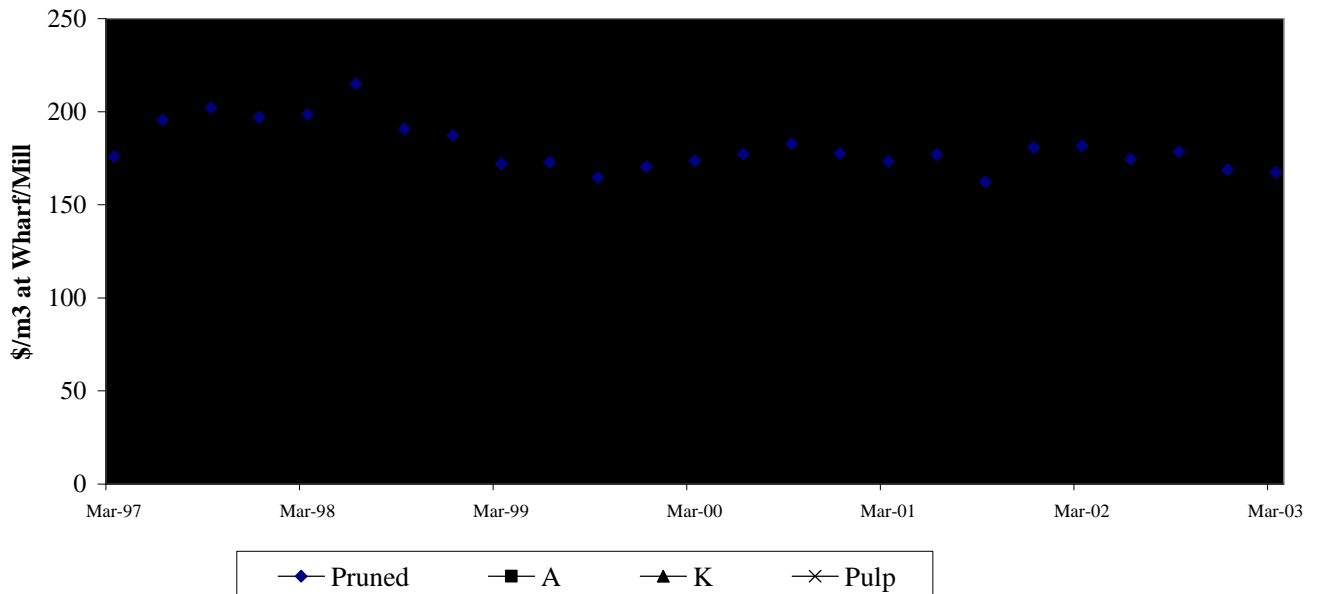
Domestic Markets

Domestic demand for all log grades is weak. New Zealand pruned log prices have fallen because of declining demand for processed pine clearwood in the United States and intense competition from South American suppliers. The South American countries supplying this clearwood market have currencies that are weakening against the US\$. They are able to manufacture finger jointed clearwood mouldings from knotty pine logs at lower prices than those manufactured from pruned New Zealand logs. Finger jointed clearwood mouldings compete with clear moulding mainly in the painted market segment.

The graph below shows how log prices have moved during the past 6 years. The differential in price between pruned and A Grade has remained relatively constant at just over \$70/m³, which means that pruning remains a profitable option on most sites.

The pulplog demand is very weak in both domestic and export markets. The Kinleith pulp mill is closed due to a prolonged strike and other pulpmills are curtailing pulp processing because the current high prices for electricity makes its manufacture less profitable.

LOG PRICES 1997-2003 (CPI adjusted)



Location	Postal Address	Office Address	Phone	Fax
Rotorua (Head Office)	Peter Clark (CEO) P O Box 1127, Rotorua	430 Ngongotaha Road	(07) 357 4135	(07) 357 5185
Far North	Bob Shirley P O Box 633, Kaitaia	228 Commerce Street	(09) 408 0480	(09) 408 2974
Mid North	Peter Bullen P O Box 322, Kawakawa	62 Gillies Street	(09) 404 0032	(09) 404 0455
Gisborne	Nick Bunting P O Box 516, Gisborne	396 Childers Road	(06) 868 5426	(06) 868 4147
Hawke's Bay	Bob Pocknall P O Box 824, Napier	72 Ford Road, Onekawa	(06) 834 3871	(06) 834 3872
Wairarapa	Phill Wishnowsky P O Box 2059, Masterton	Cnr Dixon & Crayne Streets	(06) 377 3531	(03) 377 2913
Nelson	Peter Wilks P O Box 3353, Richmond, Nelson	195A Queen Street, Richmond	(03) 544 0066	(03) 544 0067
Marlborough	Rob Lawrence P O Box 282, Blenheim	Marlb. Research Centre, SH1	(03) 577 6675	(03) 577 6674
Southland/Otago	David Thode P O Box 975, Dunedin	Unit 12, No 4 Strathallan St	(03) 455 8995	(03) 455 0107
Olsen Seed	Wei-Young Wang P O Box 1127, Rotorua	430 Ngongotaha Road	(07) 357 4135	(07) 357 5185
E-mail:	info@pfolsen.co.nz or firstname.lastname@pfolsen.co.nz	Internet:	www.pfolsen.co.nz	

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