AMURI HILLS FOREST PARTNERSHIP
Forest & Joint Venture Particulars
+ 2016 Annual Report

Partnership Particulars

Year Established	1995
Number of Partners	47
Main Assets	219 hectares of plantation forest in 5 stands
Management Committee	Warren Forestry Ltd, J McCaul, GTG Kingston, DS Lawrence
Forest Manager	Warren Forestry Ltd
Accountants	Bartram's
Auditor	Grant Thornton
Bank	ANZ Bank
Independent Forestry Consultant	Patrick Milne, NZIF Registered Consultant
Supervisor	Covenant Trustee Services Ltd

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Nature of Business

The sole business activity of the Partnership is to grow and then harvest a plantation forest in five forest stands on land provided pursuant to Joint Venture Agreements ('JVAs') by three landowners in North Canterbury. The JVAs provide Forestry Rights, which are registered on the landowners' titles, enabling and requiring the Partnership to establish, tend and manage forest regimes for one rotation on the land. At harvest, net forest proceeds are shared between the partnership and land owners with the split ranging from 73/27% to 85/15%. That split is fixed from the start by agreement and is arrived at from an assessment of the forest sites' merits, principally the cost of forest establishment and silviculture, likely forest growth & yield, and likely harvest costs. The joint venture ends at harvest or sale of the forest and the Partnership is dissolved.

Outline of Land, Forest Location, Species, Regimes & Joint Venture Shares

Glens of Tekoa: 7,800ha sheep & beef farm north of the Hurunui River inland of Culverden, North Canterbury foothills owned by W & G McRae.

GT1: 22ha Radiata pine (seed lot GF17 seedlings) planted in 1995; 20ha clearwood regime, i.e. high pruned and thinned, to 330 sph (stems per ha); 2ha framing regime, i.e. unpruned. Expected harvest is about age 30 in 2025, but could be a few years earlier. Partnership/Landowner shares: 73/27%.

GT2 & GT3: 20ha & 39ha Douglas-fir (seed lot Eyrewell) planted in 1995, framing regime, unthinned and averaging about 1000 stems per hectare, which is high but the Consultant's advice is not to waste thin it, as that would not be cost effective. Expected harvest is about age 40, which would be 2035. However there could be a production thinning at some point if it becomes feasible. Shares are 80/20% & 85/15%.

LH1, 2016 **Radiata pine aged 21**

Leslie Hills: 3,440ha sheep & beef farm north of the Waiau River, south of Hanmer Springs, North Canterbury foothills owned by E Rutherford and family.
LH1: 110ha Radiata pine (seed lot GF17 seedlings) planted in 1995; 93ha clearwood regime, with 68ha high pruned & thinned to 340sph; & 25ha part pruned, thinned to 500sph; 19ha framing regime. Expected harvest is about age 30 in 2025, but could be a few years earlier. Shares: 79/21%.

Hopefield Station: 2,000ha sheep & beef farm northeast of Waiau, North Canterbury foothills owned by M Satterthwaite.
HF2: 27ha Radiata pine (seed lot GF17 seedlings) planted in 1995; all clearwood regime, thinned to 340sph. Expected harvest at about age 30 in 2025, but could be a few years earlier. Shares: 76/24%.

Other General & 2016 Specific Information

Insurance & Valuation: The forest is insured for fire and storm losses, firefighting costs and levies, clearance and replanting costs, earthquake and Public Liability. All cover has excesses or upper limits judged as reasonable by the Forest Manager in consultation with the Independent Forestry Consultant. Taken into account in choosing the various heads of cover, apart from cost is the lower risk gained by having the forest in five separate stands, of two species on grazed farmland not publicly accessible.

The policy is tendered annually by forest management and consultancy firm PF Olsen Ltd, the largest forest manager in NZ, as a group insurance plan for its many clients.
As part of the insurance contract service, Olsens provide a free valuation based on area, location, age, species and the regime of each individual forest stand.
As this value is 'broad brush' we compare it to a value arrived at by the Forest Manager and Independent Forestry Consultants' valuation calculator. This uses actual forest data which specifically produces forest stand values for the Partnership's forest, based on a growth model. This is straight forward to update annually.

The method used, is the same as Olsen's but from more detailed and specific information about our forest stands. It uses discounted cash flow from a calculation of forecast net harvest proceeds. Getting to that figure involves making several significant assumptions or 'judgment calls', the discount rate being the most significant. It is regarded in the industry as the best method for mid-rotation valuation even though it is by its nature quite theoretical, and the further out the more so. Forests are unusual and quite variable assets and there are insufficient sales of similar immature forests to give forests a market valuation, which if it existed would be better.

The insurance year runs from June to May so the sum insured is set in May. The insured value is an agreed value with the insurer. It does not have to be exactly Olsen's or the Consultant's forest value. It just has to be 'within acceptable boundaries' so probably could easily be 30% higher or lower, which would of course be reflected in the premium.

Actual sum insured for 2016/17:	$2,149,700 (total fire cover)
Olsen's Insurance value for 2016/17:	$2,389,215
Forest Valuation as at 31/12/15	$2,197,386
Forest Valuation as at 31/12/16	$3,120,494

Wind storm cover (the maximum offered)	$1,000,000
Fire Fighting cover (the maximum offered)	$1,000,000
Public liability	$2,000,000

Earthquake	$250,000
Clearance and replanting cover	$2,500 per ha
Claims costs cover	$10,000

The Emissions Trading Scheme ('ETS'). In 2010 the Partnership's forest was registered under the ETS and received carbon credits, known as NZUs, until leaving the ETS in 2014. That was done to avoid having to return those NZUs in due course, as the rules required.
This has been a significant windfall and we have paid for all outgoings for the last three years by selling down our NZUs. Late in 2016, after considering the views of many Partners, the Management Committee decided to sell most of the Partnership's NZUs, to lock in their value as there was no certainty at all about that. From the proceeds $1,000 per unit was distributed leaving enough cash for approximately three years of Partnership expenses. Accordingly another distribution could be considered, as the remaining NZUs we have are currently worth over $100,000.

The ETS continues, and is being reviewed for reforms which should keep the NZU price up and be favorable to forestry. But that was what we were told previously and it certainly was not true, with some exceptions such as our 'windfall'.
However we will re-join later in 2017 and not miss out on any of the NZUs we are entitled to as the current allocation period is 2013 to 2017. If we rejoin in that period we will get all credits earned from 2013 on. There is no longer an arbitrage opportunity but who knows what others may arise. It remains an option for us to take an income from carbon credits and then see what happens as we approach harvest age. However that would require a new agreement with our landowners which may or may not be feasible. But we must seriously look at it again. The fact that the Partnership has Douglas-fir which not only has a longer normal rotation but can be grown indefinitely is a considerable advantage. In theory we could earn more from carbon credits than log sales, or even have both.

Forest Management and Partnership Administration. Warren Forestry Ltd carries out all forest management work for both parties to the joint venture. Important forest matters are decided in AGMs or by the Independent Forestry Consultant pursuant to the Partnership's Deed of Participation and Joint Venture Agreements.
The Partnership's Manager is its Management Committee which resumed a formal management role in 2016. So the Partnership is effectively self-managing now which means it is no longer regulated as a Managed Investment Scheme by the Financial Markets Authority.

Statutory Supervisor & Auditor. The Statutory Supervisor became 'the Supervisor' in 2016 following a change to the Partnership's Deed of Participation, with effectively the same role and will continue to hold the Forestry Rights and NZUs as trustee. We appointed Grant Thornton as our new Auditor. Once the 2015 and 2016 audits are completed under the 'Tier One' auditing rules the Partnership will be able to select a less expensive and more fit for purpose audit from 2017 onwards.

Markets for Logs & Forests - General Comment. In 2016 log markets have mostly been quite good and ended the year higher than 12 months before. Chinese demand has held up well and not been so volatile. The log market is almost entirely export dependent, since 90% of NZ production is exported either as logs (50%) or product processed to some degree. The value of the NZ dollar is another significant factor and that has been down a bit. Shipping costs are very low and fuel costs which affect harvest and transport costs are lowish. Harvest and transport is still relatively costly so we hope new technology will lower these in future, and or log prices rise.
Overall the effect has been to significantly increase the forest valuations as at 31 December 2016, as they are based on expected harvest revenue, discounted back to now.

Comparison of Budget to Costs

Actual Expenditure compared to the 2016 Budget		
Operating costs	**Budget**	**Actual**
Accountant's fees	2,000	2,000
Auditor's fees	1,800	2,500
Bank charges	-	148
Carbon credit and MC work by WFL	-	1,000
Contingency	1,500	-
Deed amendment work by WFL	-	1,000
Filing Fees	-	309
Forest Inventory & Modelling	2,000	2,050
Forestry Consultant	350	-
Insurance	5,500	6,078
Legal fees	-	1,667
Management & Administration by WFL	3,950	3,950
Statutory Supervisor & FMA annual fees	2,100	1,500
Subscriptions	-	100
Track maintenance	500	500
	19,700	22,802

Notes:

Accountancy & Audit. We would like to reduce these but the financial reporting rules we are subject to prevent that currently. Mostly this is the unreasonably involved auditing requirements mentioned above. We hope that from the 2017 audit onwards the costs will be lower.

Carbon credit and MC work by WFL. Considerable extra work relating to our NZUs was required to decide formally what to do with them and then to sell most of them and distribute some of the proceeds. To date the Partnership has received just under $300,000 from selling NZUs.

Deed amendment work by WFL + Legal fees. The Partnership resolved to amend its Deed in late 2016 to take it outside the jurisdiction of the securities law and become an independent private partnership. This required seeking legal advice and work from Anthony Harper, and liaising between them and the Supervisor. Warren Forestry Ltd did a lot of the routine drafting work together with Anthony Harper. It also required an Extraordinary General Meeting to approve the Deed of Amendment.

Forest Inventory & Modelling. Inventory work is taking plot samples from the forest stand to update our database. Then we put this in the forest growth modelling software we use called 'Calculator'. That then in turn provides a volume and log grade forecast at harvest which is fed into the valuation calculation spreadsheets.

Charles Etherington
Warren Forestry Ltd
Forest Manager & Administrator for the Partnership's Management Committee
March 2017