

# INSIGNIS FOREST PARTNERSHIP

## Forest & Joint Venture Particulars

### + 2019 Annual Report

#### Partnership Particulars

Year Established	1996
Number of Partners	70
Main Assets	275 hectares of plantation forest in 3 stands
Partnership Management Committee	P Methven, M Tillman, D Barker
Forest Manager	Warren Forestry Ltd
Accountants	Bartram's
Bank	ANZ Bank
Independent Forestry Consultant	Patrick Milne, NZIF Registered Consultant
Supervisor	Covenant Trustee Services Ltd

#### Forest & Joint Venture Particulars

##### Nature of Business

The sole business activity of the Partnership is to grow and then harvest a plantation forest in three forest stands on land provided pursuant to Joint Venture Agreements ('JVAs') by three landowners, two in Marlborough and one in 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. The Partnership pays a fixed annual rent, although at harvest a small share of net forest proceeds may be due to Landowners based on a formula relating to inflation of forests costs compared to land values. The joint venture ends at harvest and the Partnership is dissolved.

##### Outline of Land, Forest Location, Species, Regimes & Land Rental - Insignis has 3 Forest Stands:

**The Ramshead:** 2,776ha sheep & beef farm north of the Omaka River, in a branch of the Waihopai Valley, Marlborough foothills owned by Paul Huddleston.

**RH1:** 82ha Radiata pine (seed lot GF28 cuttings & GF17 seedlings, 50:50 mix) planted in 1997; All in a clearwood regime, i.e. high pruned and thinned, to 380 sph (stems per ha); Expected harvest about age 29 (2026). Site rental is \$64.61 per ha per annum.

**Chimney Creek:** 800ha sheep, beef & cropping farm in the Waikakaho Valley, north of the Wairau River, inland of the Picton road, Marlborough. Owned by Pat & Mary O’Sullivan.

**CC1:** 156ha Radiata pine (seed lot GF28 cuttings & GF17 seedlings, 50:50 mix) planted in 1998 & 1999; 140ha clearwood regime, i.e. high pruned and thinned, to 380 sph (stems per ha); 16ha framing regime, i.e. unpruned, but thinned to 550sph. Expected harvest about age 29 (2027). Site rental is \$70 per ha per annum.



**Paratu Forest, May 2019.** Note bare ground under dense areas of trees. Many wrongly think pines deplete the soil to cause this. Pure myth. They dominate the light completely, and in drier parts, moisture too. Hence good grass where it’s more open. They actually improve average soils.

**Paratu:** Sheep & beef farm south of Waimate, South Canterbury downs, owned and farmed by Jason & Nicola Cooney.

**PT1:** 33ha Radiata pine (seed lot GF28 cuttings) planted in 1997; all clearwood regime, thinned to 390sph. Expected harvest about age 29 (2027). Site rental is \$100 per ha per annum.

## **Annual Report**

### **General & 2019 Specific Information**

**Forest Growth & Health:** All was well in 2019. The three forest stands are healthy and were not affected adversely by any weather or climatic events. They are growing vigorously.

**Insurance & Valuation:** The forest is insured for fire and storm losses, clearance and replanting costs, earthquake and Public Liability, plus for claims costs (NB: firefighting costs are now covered by the state). All cover has excesses or upper limits judged as reasonable by the Forest Manager in consultation with the Independent Forestry Consultant. It is a judgement call choosing the level of cover. Both cost and risk are relevant. The insurer does not give us a discount for the lower risk gained by having the forest in separate stands, mostly bordered by grazed farmland, in the ley of hills and without public access.

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. We find it the best policy. 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 arguably be better.

The insurance year runs from June to May so the current sum insured was set in May 2019. The insured value is an agreed value with the insurer. It does not have to be exactly Olsen's or our forest value. It just has to be acceptable to the insurer so probably could easily be 50% higher or lower, which would of course be reflected in the premium.

We decided to insure above the then current valuation (31 Dec 2018) in case values kept rising up to 30 May 2020. As it happened, they fell in June 2019, then largely recovered by end of year, and have slumped since.

So arguably, at time of writing we are over-insured... Which is better than the opposite.

Actual sum insured (total fire cover)	\$7,615,600
Olsen's Insurance value for 2019/20	\$7,180,048
Forest Valuation as at 31/12/18	\$7,325,838
Forest Valuation as at 31/12/19	\$7,911,905
Wind storm cover (the maximum offered)	\$1,000,000
Public liability	\$5,000,000
Earthquake	\$250,000
Clearance and replanting cover	\$3,500 per ha
Claims costs cover	\$10,000
Insurance cost June 2019-May 2020	\$21,626

**The Emissions Trading Scheme ('ETS').** In 2010 the Partnership's forest stands were registered in the ETS. The Partnership received carbon credits, known as NZUs, until leaving the ETS in 2014 and returning cheaper European credits to the government instead of our NZUs. That was done to avoid having to return these first five years of NZUs at harvest, as the rules would otherwise require. That turned out to be a significant windfall and we received enough cash by selling down our (old) NZUs yearly to cover all outgoings for a few years.

In December 2017 our application to rejoin was accepted for RH1 and PT1 but not CC1. This time MPI were not convinced CC1 was not forest land in 1990, which is a requirement. This is possibly incorrect so we will try again in 2020. Mostly reapplying will fail but we should try, especially for the



landowners, as it affects the second rotation ETS options for them very significantly indeed.

A long review of the ETS ended in 2019 and significant changes have been announced which come into effect in 2021. Unfortunately, the new rules which allow up to half of the credits received to be retained beyond harvest, so long as there is a replant, do not apply to any of this Partnership's forest stands. They are too old. However, there is a new 'Permanent Forest' option which JV forest owners, could both benefit from.

Joining in 2017 meant we got all credits earned from 2013 to 2017, and then indefinitely. There is no longer an arbitrage opportunity and it is unlikely to occur again. It remains an option for us to take an income from these (new) carbon credits and then see what happens as we approach harvest age. However, that would require a new agreement with our landowners which may not be feasible. But we will seriously look at and advise on that option. In theory we could earn as much from carbon credits as log sales, and delay harvest or even have some of both. Any changes to this investment will require investor and landowner consent at a very high level, which is unlikely unless it is very low or no risk.

**Forest Management and Partnership Management & Administration.** Warren Forestry Ltd remains Forest Manager and Partnership Administrator for the Partnership's Manager which is its elected Management Committee. Important forest matters are ultimately decided in AGMs with advice from the Manager & Independent Forestry Consultant pursuant to the Partnership's Deed of Participation and Joint Venture Agreements.

**Supervision.** The Supervisor is Covenant Trustee Services Ltd, formerly our Statutory Supervisor, with largely the same role and continues to hold the Forestry Rights and any NZUs as trustee.

**Markets for Logs & Forests - General Comment.** In 2019 log markets were consistently good until June when there was a big drop due to oversupply. But most, although not all that fall was recovered by December. Chinese demand has been strong and stable for a few years. The log market is almost entirely export dependent, since 90% of NZ production is exported either as logs (60%) or product processed to some degree. The value of the NZ dollar is another significant factor as are shipping costs. Both changed little in 2019.

Diesel costs affect harvest and transport costs which are still relatively expensive, so we hope new technology will lower these in future, and or log prices rise further to offset them.

Overall there was no prices/costs increase in forest values in 2019. So the value increase shown above is from being one year closer to harvest, as net harvest revenue is discounted back to now.



## Comparison of Budget to Costs

Actual Expenditure Compared to Budget			
	Budget 2019	Actual 2019	Actual 2018
<b>Operating costs</b>			
Accountant's fees	2,000	1,940	1,748
Bank charges	-	89	129
ETS associated work	500	500	800
Insurance	19,000	21,626	17,637
Legal Expenses	-	-	1,000
Management & Administration by WFL	7,900	7,900	7,900
Rent	19,881	19,881	19,881
Supervisor: annual fee	1,500	1,500	1,500
Subscriptions	-	-	115
Track maintenance	700	250	150
Travelling expenses	-	300	312
	51,481	53,986	51,172

### Notes:

**ETS Associated Work:** As referred to on page 3, the ETS keeps us on our toes with increasing complexity and changes. We engage an expert to advise us and attend government briefings etc. It is worth it for the Partnership, as was proved in the early days and we still think there is more to come.

**Management & Administration by WFL:** This is a fixed fee set annually to cover all time cost and mileage for all likely routine work. We work it out from looking at the previous year's hours and mileage for all six of our forest investment partnerships and making any adjustment for likely changes. Then we apportion the total to the partnerships based on forest area and adjust them again up or down depending on any expected extra work for a particular partnership.

**Insurance:** We decided to increase cover again significantly, since there was a continuing strong increase in forest value due to log price increases. Also, fire appears to be an increasing risk. The Budget was done earlier in the year.

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

**February 2020**

**PTO for some pics...**





**Paratu's tough pines: Born into a drought in Jan 1998 below. Grew into the above by 2018**

