

5 things advisors should know about forestry investment

and more

15 November 2023



Forest Enterprises[®]
Creating wealth. Naturally.

Introducing

Gordon Wong

- Legal Services Director
- Board member, Forest Enterprises Limited
- Co-owner



Graeme Tindall

- Managed Investments Director
- Chair, Forest Enterprises Limited



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Quick intro

Gordon is one of Forest Enterprises' six owners, he is the Legal Services Director.

Graeme is our Managed Investments Director and has been with the firm 27 years.

Both have a long association with the company and our clients.

Forest Enterprises is a leader in responsible forest management and is one of New Zealand's leading forestry investment managers.

- Forestry is a niche investment but is not on the fringe.
- Thousands of Kiwis are invested in forestry. It's likely one of your clients has a forestry investment and is, or soon will be, receiving harvest and/or carbon income.
- For investors who have shares in forests which are harvesting, they may turn to their trusted financial advisor to help them understand distributions vs taxable income, they may wish to transfer ownership to family members or a trust, or they may have heard about forestry as an investment option and want to know more.
- New investment opportunities have emerged in recent years from a number of investment managers, but how does it work?

A photograph of a spider web on a pine tree branch. The web is a classic orb-weaver web, with a central spiral and several concentric rings. It is positioned in the upper right quadrant of the image. The pine needles are a vibrant green, and the background is a dark, blurred green with bokeh light spots. The text "1. Niche, not fringe" is overlaid in white, bold, sans-serif font on the left side of the image.

1. Niche, not fringe

Forestry is niche, not on the fringe

- 50+ years of retail forestry investment in NZ
- Your clients may already have invested in forestry
- Our clients invest for family or retirement – Kiwis in their 40s, and have experience with investing
- Invest for diversification, longer-term returns, and hedge against inflation
- Institutional investors like forestry

- Retail forestry investment has been around for over 50 years – there are few options available in the market today
- We have 6,500 individual investors, and there are thousands more with similar investment managers
- It's likely you have a client with a forestry investment, especially if they're at or approaching retirement
- Our clients invest for family or retirement, are typically kiwis in their 40s when they first invest, and have some experience with investing – this is true of our investor profile in the 1990s as well
- Forestry helps to diversify an investment portfolio and balance it towards sustainability; hedge against inflation; longer term returns
- Institutional investors, like superannuation funds, like to invest in forestry for these reasons as well



2. Pros & cons

Advantages of forestry investment

- Returns linked to forest product prices
- Versatility of timber products and global demand
- Ethical investment classification, environmentally sound, tangible
- Wide timeframe for harvest
- Monetisation of carbon under ETS
- Diversified portfolio and market risk
- Tax deductibility
- Professionally managed, passive investment



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The most important distinguishing features are:

Advantages

- An investment with returns linked directly to international prices for forest products
- Ethical investment classification
- A wide timeframe over which the forest can be harvested, which allows the forest to be carried forward over periods when markets are less favourable
- Versatility of end uses for timber, which diversifies the market risk
- Monetisation of carbon under the ETS, which diversifies the market risk
- Prices of logs have historically kept up with inflation and forestry investment is still generally recognised as a hedge against this.
- The historical world demand for timber is closely correlated with a combination of population and gross domestic product growth
- There are taxation advantages, both through deductibility and deferral of taxable income until the end of the project
- An investment that can be professionally managed
- An investment well suited to spreading risks in a balanced investment portfolio
- A traditional, tangible investment that has not been undercut by rapid changes in technological

developments

- An environmentally sound renewable resource and the capacity to sequester CO₂.
- A cashflow that suits superannuation goals
- The ability to be closely involved with a tangible biological investment
- Recreation opportunities.

Risks

- Long-term in nature
- Characteristics of global and local demand
- Biological
- Climate
- Fire
- Financial and operational

As with all investments, there is risk with forestry investment.

Risks / Disadvantages

- The investment is long term in nature, as radiata pine in New Zealand will require a rotation of typically 25 to 30 years before maturity is reached
- In most forest growing investment ventures, any income prior to forest maturity will be minor unless there are available carbon credits to sell
- The cashflow profile of forest growing requires an ongoing funding commitment during the establishment and tending phases.
- Future markets 25 to 30 years ahead are impossible to predict so market risks may be significant. Market returns are affected by substitution from other products, input costs (including freight rates to get wood to markets), the exchange rate.
- Global and country specific economic growth factors strongly influence the demand for wood products for uses such as building and housing, furniture and fittings, packaging or other industrial use.
- Biological risk exists – pests and disease, although New Zealand has to date shown a commitment to research and border control to mitigate this
- Climatic risk including wind, floods, landslides and storm damage – Cyclone Hale and Cyclone Gabrielle this year are examples of the impact of natural disasters on forestry. Insurance can partially mitigate this risk, and good establishment and silvicultural practices will reduce it

- Fire risk – most forest owners insure against this
- Financial risk due to changes in taxation policy



3. Not all are created equal

Not all forestry investments are the same

- Look for the protections offered by the Financial Markets Conduct Act 2013
 - Licensed manager
 - Supervisor
 - Independent auditor
 - Disclosure

The legal environment for forestry investment

The most important piece of legislation relating to forestry investment is the Financial Markets Conduct Act 2013.

Financial Markets Conduct Act 2013 (FMC Act)

- This Act regulates offers of 'financial products'. It ensures protections are in place, including prescriptive disclosure requirements, to support fair, efficient and transparent financial markets. Certain disclosure obligations will apply if an offer is a 'regulated offer' of financial products, essentially arising where the offer involves retail investors.
- The FMC Act also implements fair dealing rules for financial products and services, which apply to both retail and wholesale clients. The Act creates registration and governing document requirements for regulated offers of managed investment schemes. It also creates a licensing regime for managers of registered managed investment schemes.
- With the contributory nature of forestry investment and the longer term horizon from planting of seedlings until harvest of the tree crop, on average around 26 to 28 years, the most suitable structure for affordable forestry investment at the retail level is a limited partnership. This has the benefits of limited liability which a company has, but unlike a company (other than a smaller look through company), losses can be deducted against other income and are not trapped in the company. It also enables funding by calls to be made from investors, typically on an annual basis to meet the ongoing silviculture costs.
- Limited partnerships fall into the category of managed investment schemes under the FMC Act. Therefore, if a forestry managed investment scheme is offered to retail investors it will need to be registered on what is known as the Disclose Register and is subject to disclosure and governance requirements under the FMC Act. The manager of the scheme must be licensed and an independent supervisor (trustee) must be appointed.

- Unless one of the exemptions in the FMC Act applies, an offer of financial products in a forestry managed investment scheme to retail investors requires a Product Disclosure Statement (PDS). A PDS provides a potential investor with essential information to help them decide whether to invest in a financial product. It uses clear language to explain the product and how it works, and provides information about the business that is offering it. Importantly, it will give an investor an understanding of the risks and returns and the fees and charges involved in the investment.
- Information on a registered forestry managed investment scheme will also be publicly available on the Disclose Register website, which will include audited financial statements, governing documents of the scheme and how the scheme is managed (e.g. there is a requirement for a Statement of Investment Performance and Objectives). The financial service providers must keep this information up-to-date while they continue to offer the financial products, so investors can check online for the latest scheme and product details.

Not all forestry investments are the same

- Timber, carbon or both?
- First or second rotation crop?
- Investment structure
- Land ownership
- Active or passive management
- Third party asset manager
- Fees

- Timber and/or carbon – second rotation investments are a blend of timber and carbon
- First vs second rotation – pros and cons depending on whether a forest is already established, or newly planted; Forest Enterprises’ new investments are established forests under management, replanted for a second rotation
- Structure – LP and its benefits (others have unit trusts, companies)
- Our investments include ownership of the land which has a number of benefits
- Forestry asset – timber, carbon credits, land and environment – we are a full-service provider, meaning we do not engage a third party asset manager
- Fees will depend on investment structure and management approach



4. Cashflow

How the cashflow works

- Income from carbon
- Income from sustainable harvest
- Distributions and taxable income
- Calls payable - expenses and tax benefits
- Valuations – treecrop, land

- Income from carbon – from around 2030 in second rotation forests via sale of NZUs earned under sawtooth model; returns impacted by value of NZU at time of disposal
- Income from sustainable harvest – distributions are paid approx. quarterly; returns from harvest depend on cost of inputs (largely labour and diesel) and by domestic and international log prices
- Distributions and taxable income – income is payable by investors on their share of the investment’s income; because some income is retained to meet future expenses, distribution payments are made depending on available surplus cash
- Calls are payable by investors each year to meet budgeted annual expenses. With the Bideford Forest Investment, calls fall 2025-2029 before income from carbon commences; tax deductions are available to investors against their total income; our investments are not PIEs, investors need to declare their income each year.
- Valuations – discounted cashflow



5. Investors have options

There is an exit, investors have options

- Shares can be transferred
- Or sold
- Implications for exiting early

- Exiting a forestry investment early is possible, such as via share transfer to other family members – investors can be individuals, trusts, companies or partnerships; this is already occurring with existing clients transferring to younger family members or family trusts
- Secondary market available – early disposals are normally due to changes in circumstances
- Implications for exiting early – impact on overall return, tax/cost of timber, secondary market is subject to tender and offers will reflect potential buyers' approach to risk and market conditions



A little about us...

Forest Enterprises[®]
Creating wealth. Naturally.

About Forest Enterprises



- 50+ years in business – est. 1972
- 6 owners, 32 staff in total
- Live near our forests - Masterton (HQ), Hawke's Bay and Gisborne
- Licensed MIS manager - \$450 AUM (we don't meet CRFD threshold)
- Only FSC certified MIS in NZ
- Full-service forestry and investment management under one roof
- Actively harvesting and re-syndicating



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- Celebrated our golden anniversary in 2022. We were established in 1972 in Masterton, grew a little in the 1980s and grew a lot in the 1990s.
- Until around 2018 we were a 'small' business, we're now a 'medium' sized business – 32 staff.
- We have remained a locally owned and operated company, with 6 shareholders/directors who work in the business.
- We live where we work – this access and accountability to our communities is fundamental to our success as a responsible forest asset manager.
- We are licensed to manage Managed Investment Schemes (excluding managed funds) which are primarily invested in forestry assets. We currently have 53 x MIS.
- We hold Forest Stewardship Council® Forest Management certification (FSC-C168647) for responsible forestry. Ours are the only MIS in NZ to be FSC certified.
- We are a full-service manager with forestry and investment management under one roof, comprising legal, finance & accounting, technical forestry, harvesting, GIS, valuations and modelling, and client services staff.
- We have a large active harvest and replant program – approx. 1m tonnes p.a. for all forest under management. We manage approx. 35,000 hectares in total in Gisborne, Wairarapa and Hawke's Bay.
- We are actively re-syndicating the forests to the next generation of investors. After harvest, we are offering new-issue investments with a mix of timber and carbon investment income from second rotation forests, eg Bideford in Wairarapa.

Bideford Forest Investment



- Minimum initial investment cost \$10,078 / 200 shares ('unit') (\$50.39 per share)
- Total calls \$3,099* / unit (2025-2029)
- Return \$121,809* / unit, 14% IRR
- Carbon income from 2030
- Harvest income 2047 and 2050
- Product Disclosure Statement – Disclose Register or [forestenterprises.co.nz/bideford](https://www.forestenterprises.co.nz/bideford) for cashflow and assumptions, risks, how the investment is structured and managed

** Per 200 shares, adjusted for 2% per annum inflation and before tax. Based on Forest Enterprises' 36-month average log price series to 30 September 2022 and a price of \$80 per carbon credit. Refer [Product Disclosure Statement dated 25 November 2022](#) for cashflow projection and assumptions.*

For a copy of the product disclosure statement, download here:

<https://www.forestenterprises.co.nz/downloads/21291/>



More information



Helpful resources about forestry and forestry investment

- Investing in forestry – forestenterprises.co.nz
- Companies Office Disclose Register – companiesoffice.govt.nz/disclose
- Forest Enterprises’ harvest management practices – [Good Practice Guideline for Catchment Management on the East Coast](#)
- Wood: our low-carbon future – woodourlowcarbonfuture.nz
- Forest Owners Association – “Facts & Figures” – nzfoa.org.nz
- Te Uru Rakau | New Zealand Forest Service – mpi.govt.nz/forestry



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- Forest Enterprises team is available anytime: 0800 746 346, info@forestenterprises.co.nz
- Disclose Register – for governing documents and annual reports
- Forest Enterprises co-owner and Gisborne Regional Manager, Dan Fraser lead the development of Good Practise Guidelines for harvesting on the East Coast, based on his harvest management techniques deployed in Forest Enterprises’ Gisborne forests over the last 5-6 years.
- Forestry sector websites

Thank you!

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