

Log Market Analysis

As at 4 May 2020



Photo 1: Brolly Logging back on the job, Wairarapa

The content of this Log Market Analysis is produced monthly as part of a suite of documents that comprise the regular reporting to forest owners during harvest. This standalone document is made available to other forest owners approaching harvest to keep them informed on market conditions.

We have included log price series separately for Wairarapa and Gisborne forests, as the price series differ for reasons including different customers, log specifications and locations.

Forest Enterprises (FE) is currently harvesting approximately 650,000 tonnes of logs per annum for Wairarapa and Gisborne forest owners. We now harvest and deliver a further 350,000 tonnes for a private fund manager client in the same regions.

Our harvest volume was very low in April as we deal with the Covid-19 crisis, but we have restarted production.

IMPORTANT

Every effort has been made to provide current accurate information in this document, which is for information purposes only. Any opinions and views expressed are those currently held by Forest Enterprises, however the reader accepts that where they are opinions and views in respect of future prices, they may subsequently be proven incorrect. The nature of the international log market is that of price fluctuations, and these fluctuations can be material, and material changes can arise due to factors not previously able to be foreseen.

Overview

It has been a long time since I last spent four weeks at home not fully occupied, and that's probably common to many of us. I have tidied my workshop and organised the nails by size in different containers. With the time left to me, I took to literature and am deeply into Moby Dick. I'll offer a quote:

"I know not all that may be coming, but be it what it will, I'll go to it laughing."

– Herman Melville, *Moby-Dick / The Whale*

It's worth remembering that Moby Dick's central themes included insanity and poor judgement of risk.

We are all dealing with life as it comes, and it feels for us here in forestry it has been coming rather slowly. Contractors will be suffering losses as they have had wage payments to make, and sawmill customers have log stocks uncut and unsold. Many people find themselves in difficult situations in these trying times and I recognise that.

If it is any consolation to investors, I can state that forest investments at this point are not badly affected. We have lost time; the lost time has an effect on cashflow and, in turn, the amount able to be distributed in the coming quarter(s). In the meantime, the trees that would otherwise have been harvested remain standing, growing in size and value.

I can reassure investors that the log market is functioning, and that customers have paid and continue to pay for logs.

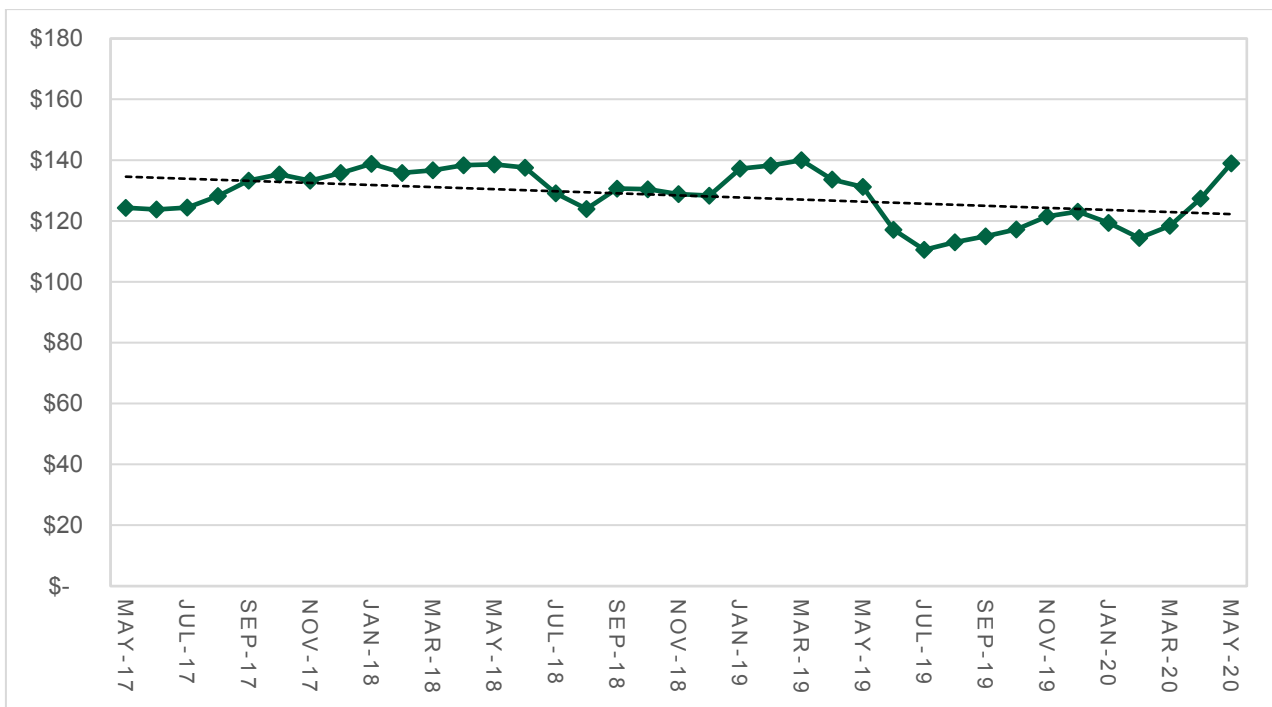
I wish everyone all the best in these tough times.



Wairarapa Log Prices Per Tonne

Grade	Forest Enterprises Apr-20	Forest Enterprises 36 Month Average	Current vs 36 Month Average	Percentage of the 36m Average
Export P40	\$195.90	\$183.90	\$12.00	107%
Export P30	\$154.10	\$145.20	\$8.90	106%
Export A	\$129.00	\$133.40	(\$4.40)	97%
Export K	\$114.55	\$118.20	(\$3.65)	97%
Export KI	\$106.70	\$111.45	(\$4.75)	96%
Export Pulp	\$93.50	\$96.20	(\$2.70)	97%
Domestic P35	\$170.00	\$175.20	(\$5.20)	97%
Domestic S30	\$117.00	\$121.15	(\$4.15)	97%
Domestic S20	\$102.00	\$106.15	(\$4.15)	96%
Domestic Pulp	\$31.00	\$31.00	\$0.00	100%
Export sales units are volumetric (JAS) while domestic sales units are paid per tonne. The Export JAS prices have been converted to tonnes. Refer to page 5 for more detail on the JAS to Tonne Conversion.				
Index Log Price	\$127.35	\$128.15	(\$0.80)	99%
Index Log Price is calculated using inventory measurements from our Wairarapa forest crops and establishing an average log grade recovery for our typical Wairarapa Forest. Applying these estimates to our long run prices per grade has derived an Index Log Price. This index price helps to estimate the average logs sales predicted for a typical forest.				

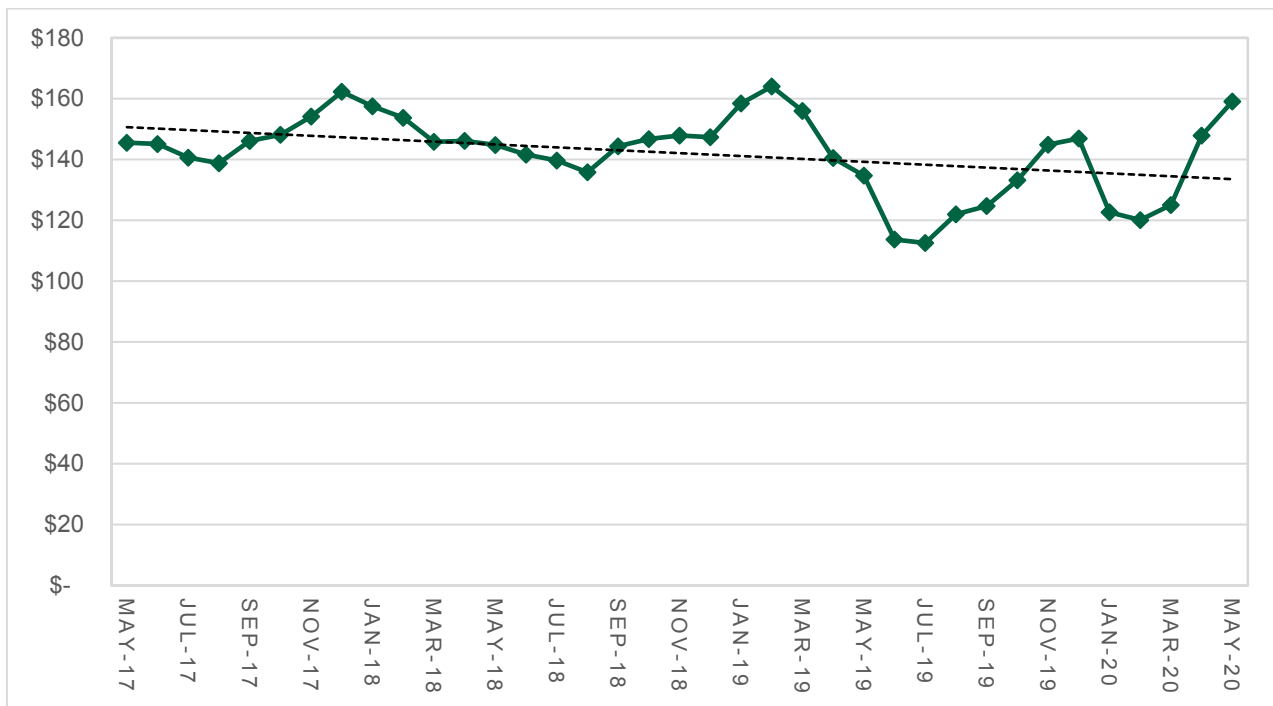
Index Log Price for our typical Wairarapa Forests



Gisborne Log Prices Per Tonne

Grade	Forest Enterprises Apr-20	Forest Enterprises 36 Month Average	Current vs 36 Month Average	Percentage of the 36m Average
Export P40	\$191.10	\$181.30	\$9.80	105%
Export P30	\$149.00	\$148.05	\$0.95	101%
Export A	\$147.00	\$139.60	\$7.40	105%
Export K	\$129.00	\$125.10	\$3.90	103%
Export KI	\$121.00	\$115.50	\$5.50	105%
Export Pulp	\$103.50	\$102.80	\$0.70	101%
Domestic P35	\$175.00	\$178.75	(\$3.75)	98%
Export sales units are volumetric (JAS) while domestic sales units are paid per tonne. The Export JAS prices have been converted to tonnes. Refer to page 5 for more detail on the JAS to Tonne Conversion.				
Index Log Price	\$147.85	\$141.65	\$6.20	104%
Index Log Price is calculated using inventory measurements from our Gisborne forest crops and establishing an average log grade recovery for our typical Wairarapa Forest. Applying these estimates to our long run prices per grade has derived an Index Log Price. This index price helps to estimate the average logs sales predicted for a typical forest.				

Index Log Price for our typical Gisborne Forests



NOTE: The trend shown on the charts is that Gisborne returns are more volatile than in the Wairarapa. This is largely due to the smoothing influence of the relatively large domestic sawmill market in the Wairarapa. We have added domestic customers in the Gisborne region recently which will make price less volatile.



Factors Influencing Current Log Price

Key:

↑ More Benefit to the Investor

↓ Less Benefit to the Investor

↔ Neutral

Price, Costs and Logistics

↑ Foreign Exchange (Forex)

Export logs are priced in USD. FE's rate for some volume shipped in March was 0.6335. Expectation for May forecast is at a rate of 0.6017 which is in our favour. Exchange in NZD typically falls in response to commodity price falls as investors lose confidence.

FE takes no forward position or hedge in currency trading. Hedging imposes transaction costs without giving certainty of improved outcomes.

↑ Shipping

Shipping rates are very low as there has been little activity. Shipped volumes from NZ in May are forecast to be about 50% of normal levels so shipping should stay low for the short term. Costs will rise if volumes rise as ship charterers seek to recover losses.

↑ JAS to Tonne Conversion

JAS-to-tonne conversion rates fell from very high levels to what is still high at about 104% for all export grades during April 2020. This is a good result however volumes were lower than usual, and some stock had been held and was drier and therefore lighter than normal. I expect rates to fall in May.

Export logs are sold in Japanese Agricultural Standard cubic metres (JAS). JAS is a measure of useable log volume rather than weight. Payments to most contractors are made based on weight, which is appropriate for handling heavy material. This means the return to the forest owner is affected strongly by the conversion of weight to volume in the logs.

Conversion has seasonal trends and varies between log grades, length and log quality. Accounting for conversion is necessary to report comparable values from different sales options. Our convention is to report all prices converted to the 'per tonne basis', which would appear different if compared with a per cubic metre (JAS) series. Hence why our harvest reports show monthly JAS/tonne conversion per forest.

↑ Log Price, Export CFR

CFR (Cost and Freight) is the price in USD paid by the end user/buyer.

China Price rising due to fear of missing out as Customers are aware that New Zealand production has stopped.

South Korea Low price and demand.

India Price limited by low demand for lumber.

Japan Falling demand restricts price.

Log Demand

↓ Export Log Inventory in Market

China Inventory of logs in China is a leading supply/price indicator. Inventory levels in China rose very high and then declined as New Zealand took a month out from log production. Current stocks are estimated to be down a million cubic metres or so over the month, currently about 5,000,000 JASm³, and daily usage is around 60,000 per day. Days of stock is inventory divided by usage and cannot be measured easily. It has declined to about 80 days, which is still high. The speed that logs turn to lumber and lumber turns to cash drives market sentiment. European spruce lumber has also declined, however, it is expected to reappear in the market as containers become available.

South Korea There has been a demand spike driven by inventory correction, there is no sustainable price rise.

India Sawmilling limited by Covid-19 conditions.

Japan Log and lumber consumption declining.



↑ Pruned Log Grades

After our month off, our pruned customers are eager to resume normal business.

↔ NZ Domestic

Local sawmills are firing up as fast as they can, but they are limited by the availability of fresh cut logs as many forest owners are clearing pre lockdown cut logs from stockpiles. We have high demand for fresh logs and are focussed on meeting that demand.

↓ Housing and Business

There is not much useful commentary out there, but what there is, is worrying.

It's clear that the number of people wanting homes and those selling will remain static, but what is changing rapidly is the ability to pay. Tenants are stopping rent payments and retail is dying. Airbnb is probably going to be a memory soon. So that's part of demand, but we still have families needing homes.

It's likely that prices of existing housing stock will fall; I've seen 7% forecast, who knows. The fundamental problem remains that New Zealand has a shortage of housing. I hope there is a response in building affordable accommodation, as that's the missing piece of the puzzle.

↓ Domestic Construction

Construction is shut down currently, but we badly need construction up and running. I expect it will be a big part of Government plans.

Log Supply

NZ

All harvesting stopped for about 5 weeks'; we are going again but it is time to ramp up.

Australia

Still logging as normal.

Europe and Russia

Slow in Europe.

Pacific Northwest (PNW)

Still harvesting.

Other

Still harvesting.

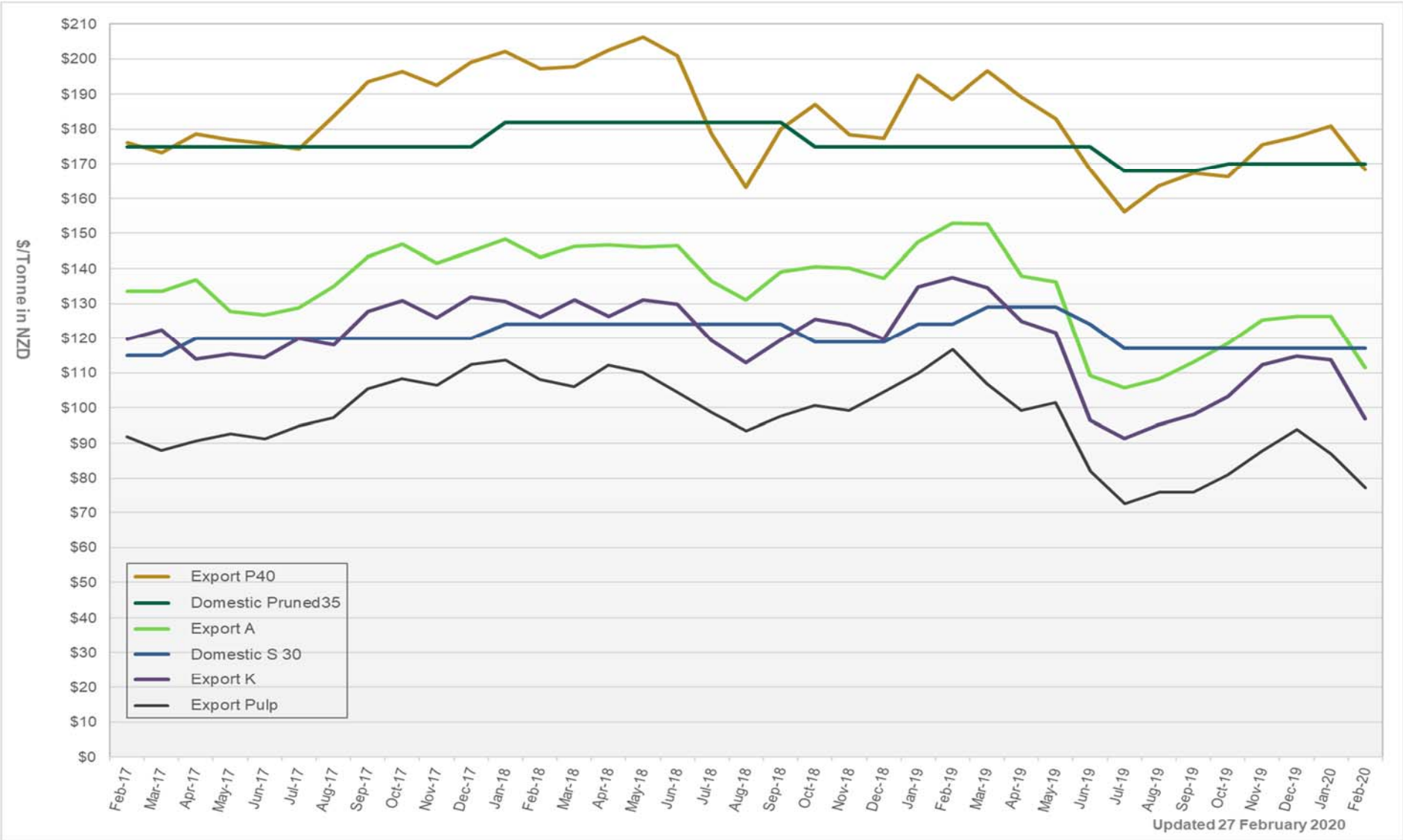
Point of Interest



With thanks to the Betoota Advocate, the doomsday switch, we hope it can be used soon.



Lower North Island Log Price Graph per Tonne



Log Price Graph: Tracks the key log prices for a 37-month period. The first 36 months are the months which comprise the average referred to under Log Prices per Tonne above. The 37th month shows the indicative prices scheduled for the current month. Export sales units are volumetric (JAS) while domestic sales units are paid per tonne. The Export JAS prices have been converted to tonnes.



NGATAWHAI GROUP FOREST INVESTMENT

We are proud to provide this opportunity to invest in a sustainable, productive future for New Zealand.

The Ngatawhai Group Forest in Wairarapa is 627 stocked hectares of outstanding pine forestry, as well as 200+ hectares of permanent native bush and wetland.

This is existing forest land Forest Enterprises managed over three decades, through to the productive harvest of the first rotation crop.

Ready planted for its second crop rotation, this forest is now available for the next generation of investors.

Investment Overview:

- Initial Investment: Minimum initial application cost \$9,726 for 200 shares, plus affordable annual contributions
- Additional shares may be purchased at \$48.63 per share
- Projected annual contributions: Calls are projected to average around \$1,011* per year for 8 years, then drop to an average of around \$291* per year until harvest commences in 2038. The first call is 30 June 2020.
- Projected total investment: \$20,797*
- Projected gross return: \$129,060*
- Projected gross IRR: 9.33%*
- Harvest period (income): 2038-2046
- Production forest 627 net stocked hectares - 2.09 hectares per 200 shares

* Per 200 shares, based on 2% per annum inflation and Forest Enterprises' 36-month log price series to 30 June 2019. Refer Cashflow on pages 28-29 and other financial information in section 6 of the Product Disclosure Statement from page 25.

To learn more and for a copy of the product disclosure statement, contact Nikki Coulmann:

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forestenterprises.co.nz/new-investments

Ngatawhai Group Forest Investment is a managed investment scheme structured as a limited partnership, offered by Forest Enterprises Growth Limited, issued and managed by Forest Enterprises Limited.

Forest Enterprises is the business name of Forest Enterprises Growth Limited and its subsidiary Forest Enterprises Limited. Forest Enterprises Limited is licensed to manage Managed Investment Schemes (excluding managed funds) which are primarily invested in forestry assets.