

Wood Matters – October 2017

Clarky's Comment – Are controls on to whom, when or at what price forest owners' sell their logs to a good idea?



Peter Clark
CEO
PF Olsen Ltd

This month's Clarky's Comment is not an original piece. It is the reproduction of an excellent article that appears as the President's Column of the New Zealand Institute of Forestry Newsletter of 9th October. It is reproduced here because Clarky happens to agree wholeheartedly with the observations made by James Treadwell.

One matter that is unclear is whether there is any expectation amongst wood processors that they would pay less for logs than owners could get by exporting those same logs. I've not heard any politician or wood processor say that. But if the controls suggested include a tax or levy on exported logs, but not on those sold domestically, then what we have is an effective discount for domestic processors, paid for by the forest owner.

I have heard of concerns that logs are being harvested "too young" and that effectively shuts domestic processors out of pricing those logs. This raises 2 issues:

1. Why are domestic processors not pricing logs based on wood properties discovered at the headrig or from sawn outturn? Technologies exist to enable that. A price differential that reflects the improved sawn timber grade outturn that comes with tree age would encourage forest owners not to sell logs that are "too young".
2. Are smaller forest owners aware of the opportunity costs associated with harvesting trees that are relatively young? Some may not be. There is probably a role for MPI or some other government agency to provide education and extension services to woodlot owners to fill this knowledge gap. Along with imparting knowledge to farmers and Maori landowners about the commercial opportunities of planting grassland under the ETS this would be a useful thing the government could do to help sawmillers on the short and longer term.

"As we wait for our Government to be formed there has been much commentary on what may or may not be the conditions of coalition. The major discussion around forestry has been the idea of forcing forest owners to supply domestic mills. This idea has been discussed on both TV1 and TV3 as well as on Radio National and various written publications.

"Whilst I am sure there are some who think this is good idea I struggle with it. Presumably being forced to sell to the domestic mills means 'at a discount' and this, I am afraid, is very short sighted. Almost all of New Zealand understands we need new and increased planting to meet many of our environmental objectives, yet this one idea would do more to stop new planting than almost anything else the Government could suggest. I know no other investment where the Government legislates the investor must sell to a processor. Where this has partially occurred (e.g. Fonterra) it has occurred with the growers' agreement and with the goal of improving returns to the grower, not reducing them.

"It has been suggested the Government could start investing in planting in its own right. At a limited scale, on Crown lands and in conjunction with iwi, this makes sense. But as we know new planting ties capital up for a long time. Any direct Government investment into new planting must compete for the tax dollar with infrastructure, health, education and social welfare. Current investment in New Zealand forestry is around \$30 billion. It is totally unrealistic for the Government to be able to replace this investment. Private investment is required to ensure we have a vibrant forest sector."

"I am a strong supporter of the need for a vibrant and strong domestic processing sector. As a sector we need this, and most forest owners recognise the need. Many large forest owners ensure they are meeting their commitments to the domestic sector before they export, and the produce they do export is mostly the grades our domestic sector does not want. What will happen to these grades? Is the suggestion we force the domestic processors to take them, even if they know they will struggle to process and on sell profitably?"

"Let us also consider our NZ Super Fund. It has a pretty significant investment in a CNI forest which has been giving them some impressive returns, partially on the back of the ability to export grades which the domestic mills don't want. It would be a pity for all New Zealanders if this particular golden goose was strangled. What this particular forest manager does is ask the domestic consumers what logs they want, then they supply them what they ask for and the left over (approximately 35% of total volume) is exported. The export volume allows this forest to be flexible with their domestic customers. Without this flexibility then I am sure this forest manager would be asking their domestic customers for a take or pay obligation, which potentially means they could be worse off with no ability to reduce input when the local markets are performing poorly."

"But let us consider the many Mum and Dads, iwi and farmers who have a small block of trees ready for harvest. As the large owners already have their commitments to the domestic processors sorted and they are long term, these poor small owners will be disproportionately effected by the requirement to supply the domestic processor as the processor will see this supply as 'additional' and therefore will not pay full price. "I wonder if the New Zealand public would support regulating apple orchards so they can't export their apples and have to sell them to the cider brewery down the road and should Watties really stop harvesting those baby peas and grow them on to full size for the good of the nation? We need to start turning our collective minds to how to encourage people to plant trees, not disincentivise!"

"If New Zealand feels strongly the wood domestic processing sector needs support, then this support should come from the tax payer in general, rather than from one part of the economy (the forest owners). There are other options to help these processors including accelerating the depreciation on machinery, the removal of overseas tariffs on sawn lumber and some of the non-trade barriers our wood processors face when exporting processed wood products."

"A strong domestic processing sector is imperative for all of us. However this should not be at the expense of the grower. As a sector we need to work together to ensure a strong processing industry exists and, in general, we do. Is it perfect? Of course not; but forcing growers to supply processors at a discount by regulating or taxing log exports will not solve the problem. In fact if this happens, in 25 years there may be very little forest to supply to any mills."

James Treadwell
NZIF President

Log Market



Scott Downs
Business Development Manager
PF Olsen Limited

Log Market Summary

The domestic log market in Quarter Four of 2017 is virtually unchanged from Quarter Three. Most mill owners reported business as usual with the usual small fluctuations in local demand due to variations in the weather.

Log prices paid by mills were generally unchanged with the occasional price increase for unpruned logs. Prices received for export logs delivered in October dropped on average \$1-\$2/JASm³ from September prices for non-pruned and \$3-4/JASm³ for pruned logs. There has been a significant and relatively unforeseen increase in ocean freight rates. This increase has averaged about US\$7/JASm³ and has been partially offset by the weakening of the NZD against the USD. Freight rates are expected to level out in November. China log demand remains steady with occasional small price increases, and October is traditionally the highest price point in the second half of the year for logs in China. The Korean log market is once again steady, and the Indian log markets shows signs of recovery. Due to the decrease in export prices the PF Olsen Log Price Index for October has reduced to \$124. (See PF Olsen Log Price Index below). The average sale price is currently \$10 per tonne above the three-year average.

Domestic Log Market

Demand

The domestic mills report very little change in domestic demand other than the usual variations due to weather. There have been a few slight changes in some export lumber markets, but these were well anticipated and had no effect on the local mills.

The domestic mills have also experienced an increase in the ocean freight costs, but have benefitted by the weakening NZD. Approximately 14% of NZ lumber exports (by value) are to Australia, and the weakening of the NZD by a couple of cents since mid-August has increased returns. These exporters however, do have to contend with one of the most expensive ocean freight costs across the Tasman Sea, ranging from \$70-\$100NZ/m³.

Log supply

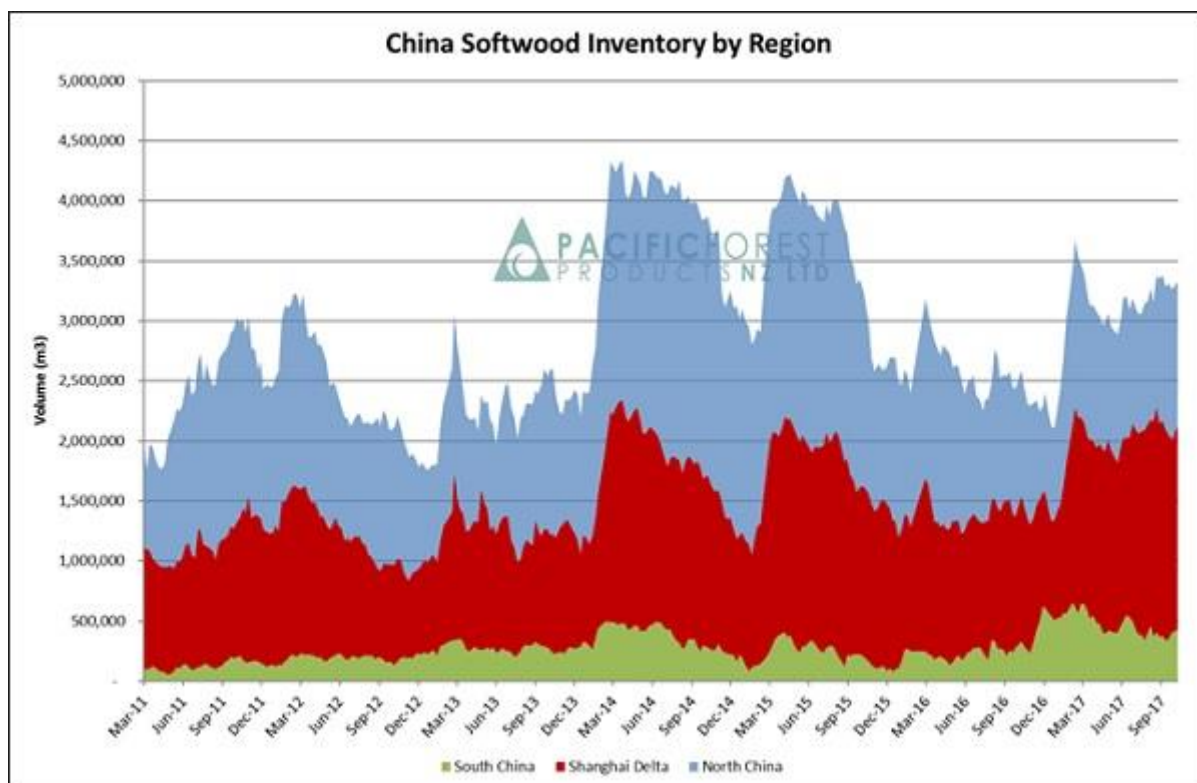
Log supply continues to be balanced around most of the country. There are some regional shortages as has been reported in the media about Northland. The mills in Canterbury are also concerned about supply going forward. This has been exacerbated by the windthrow of 2013 which removed some 1.5M tonnes of standing timber and its effect on wood-flow is being noticed sooner than thought.

Export Log Market

China

The market remains well balanced between supply and demand. The stock levels across China continue to hover around 3.3M m³, and rose only slightly during China's "Golden Week" holiday in the first week of October. The demand is still very strong across all log grades, with a healthy daily offtake of 65K m³/day. One interesting point about the current inventory in China is that the percentage of

radiata pine logs has decreased while the percentage of North American logs has increased. This is even though the supply of North American logs dropped 18% in August. This shows New Zealand logs have been more saleable than the more expensive North American logs.



Courtesy: Pacific Forest Products (PFP)

India

The Indian market has remained dull and flat for the last three months with prices hovering around US\$150/JASm³ for A Grade longs, and shipping rates touching US\$38 to \$40/JASm³ making exports to India almost unviable. The key factor for the flat market behaviour has been liquidity issues stemming out of GST upfront payment to the Indian Tax Department at the time of releasing cargo from port.

September was a slow shipment month from NZ to India with just three vessels heading to India. This caused some relief in the Kandla market, and sawn timber prices have become marginally bullish in the first half of October as log stocks have depleted. However, there will be virtually no change in the market in October, as the festival of Diwali implies working holidays and mill closures until 30 Oct 2017. The CEO for Aubade NZ (a large exporter of New Zealand logs to India) Satinder Singh expects November/December to be the turnaround period and feels a strong sentiment emerging for demand to increase as cash cycles affected by GST filing are expected to have normalised. Aubade NZ forecast the Indian log market is set to accommodate on average 5-6 vessels per month from NZ for 2018.

This augers well for log prices and supply in the period of Nov 2017–Feb 2018. This would be very welcome news as February 16, 2018 is the Chinese New Year. The Indian market could provide a good balance to keep demand reasonable.

Korea

The Korean log market is a very mature log market with no significant changes forecast. The current geo-political climate with North Korea seems to have little effect on log demand, and any demand fluctuation is mainly market driven. Kwang Won Lumber Co Ltd which is the second largest buyer of logs in Incheon, Korea, stopped buying logs in July, and logs destined for this mill were diverted to

other mills and overall demand was diminished. This mill re-commenced buying in September under court control. Due to this situation log sales to Korea in Aug 2017 were 8% down on the same month in 2016, but log sales are still 8% up on an annualised basis.

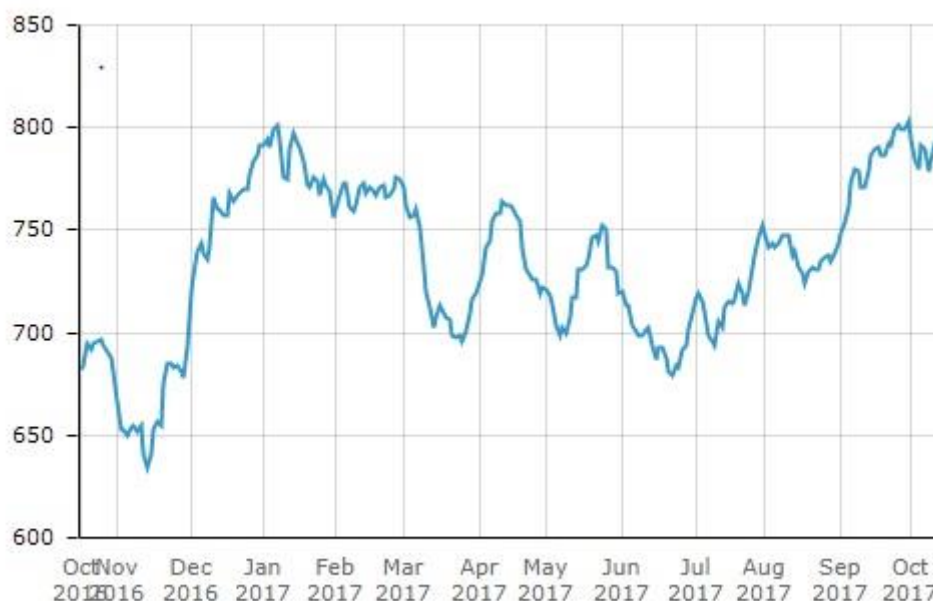
Ocean Freight

The ocean freight price to ship logs from New Zealand to China has increased by an average of \$7/m³ USD across the country. While I did report last month that “industry commentators now suggest indications are for increasing freight rates in Q4”, these increases are more than expected. The two main factors driving this recent increase in freight costs are detailed below. Most market commentators expect this to be short term and not have lasting effect on ocean-freight rates:

- There have been significant vessel delays due to monsoon and other weather events around Asia. The port of Chittagong in Bangladesh, for example, at one point had 150 ships waiting for a berth. While this port often struggles with increasing demand, that is a lot of ships! This means there is a reduction in the available shipping capacity.
- There has been a surge in freight demand due to iron ore and coal being imported to China before new stringent environmental regulations come into effect. In [last month's](#) Wood Matters PF Olsen indicated how the tightening environmental regulations may affect local saw millers and here we see another consequence of this for the NZ forest industry. While iron ore and coal tend to be shipped in the larger Capesize and Panamax vessels, the demand cascades down the dry bulk carrier fleet. Material that was shipped in Panamax carriers starts getting shipped in Supramax and Handymax vessels, and so on. The Wood Matters edition of [March](#) this year has an explanation of the freight scene for further reference.

The Bunker World Index (BWI)

The price for fuel bunker has trended upwards since mid-June of this year.



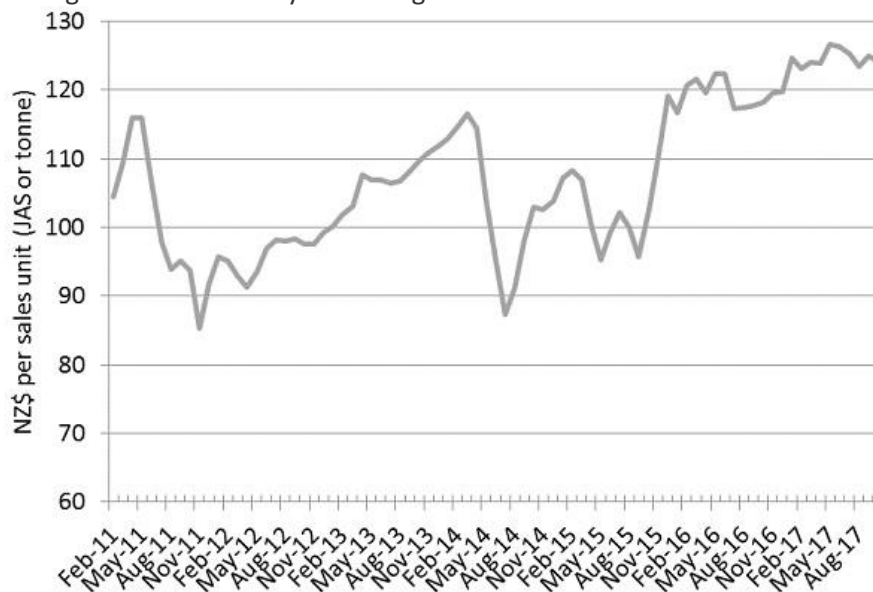
BWI graph courtesy of S&P Global Platts.

Foreign Exchange

The exchange rate continues to have a significant impact on AWG prices for logs. The NZD relative to the USD has continued to drop from the high of 0.7503 in July to 0.7179 in mid- October. This reduction in the NZD has countered the effect of rising freight costs on the 'At Wharf Gate' prices received for logs in New Zealand.

PF Olsen Log Price Index to October 2017

The PF Olsen Log Price Index for October decreased one dollar from the September index figure and is now at \$124. The index is currently \$3 higher than the two-year average, \$10 above the three-year average and \$14 higher than the five-year average.



Basis of Index: This Index is based on prices in the table below weighted in proportions that represent a broad average of log grades produced from a typical pruned forest with an approximate mix of 40% domestic and 60% export supply.

Indicative Average Current Log Prices – October 2017

Log Grade	\$/tonne at mill	\$/JAS m3 at wharf
Pruned (P40)	182	179
Structural (S30)	120	
Structural (S20)	109	
Export A		137
Export K		131
Export KI		122
Pulp	47	

Note: Actual prices will vary according to regional supply/demand balances, varying cost structures and grade variation. These prices should be used as a guide only and specific advice sought for individual forests.

Forestry and the Emissions Trading Scheme



Mike Duckett
ETS Manager
PF Olsen Limited

Domestic News

The election has been and gone, yet we are none the wiser as to what form our next government will take. I wonder as to what level climate change and ETS policy are being discussed behind closed doors. We know that both the Greens and NZ First have been in favour of replacing the ETS with a carbon tax, but is this a “bottom line”? Any attempt to unwind the ETS in its current form would be a costly and time-consuming exercise and there are likely much higher priorities around the negotiating table.

MPI has recently communicated to ETS participants the need to submit any new Post-1989 registration applications as soon as possible. An indicative deadline of 16th October 2017 has been provided, however MPI will not guarantee that applications submitted prior to this will be entered into the ETS by the 31st December 2017.

If you are considering a new registration, or adding land to an existing participation, please contact Mike Duckett ASAP.

For those ETS participants with 100 hectares or more of registered Post-1989 forest land, the deadline for submission of FMA measurement data is 31st December 2017. Inventory contractors across the country are extremely busy at present, so if you are an FMA participant and are yet to organise inventory measurement for your trees, please contact Mike Duckett to discuss.

Price Update

NZU prices started the month around \$18.30, before dropping back as low as \$17.90 immediately before the election as buyers and sellers adopted a wait and see approach. Since the start of October, prices have risen steadily to a current level of \$18.40 (as at 12th October).

Figure 1: Recent Carbon Prices - NZ\$/t CO₂e – Real (CPI adjusted)



FSC General Assembly



Kit Richards
Environment Manager
PF Olsen Limited

Positive signs for FSC Certification following and Intensive week at the FSC General Assembly in Canada.

In a unique characteristic of the Forest Stewardship Council, the organisation holds a General Assembly (GA) every 3 years. These large events include members from all three chambers (Environment, Social and Economic) from around the world, this year attracting between 500 and 600 attendees. The GA is a vital underpinning and distinguishing feature of the FSC system as it is the main venue by which the direction and policy of FSC is determined.

This year Kit Richards, Environment Manager for PF Olsen attended the GA over the 8th -14th October in Vancouver, Canada. In all there were 5 attendees from New Zealand, representing the economic, social and environmental chambers.

In summarising what was an intensive week, Kit says: “There appears to be an important transitional shift in the collective thinking of FSC and its membership which if executed should see a more positive and useful outcome for those who have trodden the FSC pathway in New Zealand for a number of years. There was evident a very pervasive undertone that the perennial issues of cost, complexity and rule-making churn must be resolved if FSC is to not only stay relevant to its current members, but to grow substantially and become much more significant in addressing the problem of poor and unsustainable forest management”.

Key observations:

1. FSC at last seems to be maturing as an organisation with an apparent trend toward the chamber members acting in a more consultative rather than political and adversarial fashion, albeit tensions were present.
2. The FSC secretariat has and is continuing to, put a lot of effort into a strategic plan, better governance and improved communication.
3. The strategic plan has correctly identified many of the issues that have made FSC so frustrating and limited growth and uptake and the chambers seem to be more prepared to accept that the objective must be to follow the plan and allow the Board the freedom to execute it without distraction.
4. The strategic plan now places large emphasis on:
 - Avoidance of continued overloading from rules and added complexity and cost.
 - Focus on simplification and streamlining.
 - Use the digital world to improve systems and transparency.
 - Increase size and market presence of FSC to make it relevant and useful to certificate holders.
 - Solve the problem of cost and complexity for small holders.
 -

5. If they can deliver on the plan FSC is likely to have a much brighter future.
6. There were 71 motions to be passed but a large proportion were withdrawn by the time it came to a vote.
7. Ultimately there was only a half dozen that had potentially serious implications for NZ. All ended in a satisfactory position.

One item that will be of particular interest to PF Olsen clients was the progress being made on a risk-based approach to pesticides management and the trial models coming out of work related to small holders. While there remains work to be done, the approaches being considered would all work to make small holder and group certification much easier and cheaper. It has been a major concern from all chambers, especially economic chambers in the US, Latin America, Scandinavia, African and Pacific Asia that this issue must be resolved and on a risk-based approach. This is encouraging news.



Democracy in Action – Voting in Progress at the FSC General Assembly in Vancouver this month.

National Environmental Standard for Plantation Forests



Kit Richards
Environment Manager
PF Olsen Limited

You may or may not be aware of the recent announcement of the passing into law of the National Environmental Standard for Plantation Forestry (NESPf).

The Resource Management Act has always had the provision to create National Environmental Standards in situations where there were very standardised processes of land management with predictable environmental consequences. It was envisaged that regulation could be made more efficient through the imposition of one national set of rules rather than different sets of rules in every council district and region.

An NES for plantation forests was one such situation and after a process involving several years the NESPf has passed into law.

The Rules of the NES will come into force on the 01st May 2018.

Up until that date there is to be an implementation and transitional period during which industry practitioners and Council planners and compliance staff can get organised to manage this new set of rules.

The NESPF has set about defining the rules that govern forestry under the RMA based on clearly defined risk. As a result, most of the rules under the NES are driven by an underlying assessment of risk related to land stability. This assessment has been formulated into a national map-based classification called the Erosion Susceptibility Classification (ESC).

There are four susceptibility classes, namely:

1. low – green zone
2. moderate – yellow zone
3. high – orange zone
4. very high – red zone.

Under the NES the rules get increasingly strict as operations progress onto higher risk zones. In many cases, the rules are less stringent than before in lower risk landscapes and very similar to current rules in high risk - orange zone landscapes.

However, in red zone terrain, the rules are tighter than anywhere previously in recognition of the fact that the industry in general is facing difficulties in these types of areas. These rules restrict planting in such areas unless great care is taken in planning the proposed afforestation, especially where it is to be in species and under management regimes that imply clear-fell harvesting.

If you are a PF Olsen client, we will be in contact with you outlining the changed regime and details of its implications. We will also be able to assist you with any queries or concerns you have and assist you integrating the new rules into the management of your forest or woodlot.

The important message is that forest and landowners with forestry operations being conducted on their land will be required to ensure that those implementing operations are conversant with the NES and that they comply with the NES.

Te Poroa Heurea - 2016 Safety Champion recipient



In most cases, forests are simply trees on hills until planning and road construction commences to enable the trees to be harvested. This preliminary activity that we call getting a forest 'harvest ready' requires a range of skills from engineering and earthworks contractors to ensure a productive and safe operation.

One of the earthworks contractors engaged by PF Olsen is Wilson Bros Earthmovers Ltd (Wilson Bros), a company with its base in Waiotahi, near Whakatane. One of Wilson Bros employees, Te Poroa Heurea (Choppy) was a recipient at the 2016 Safety Awards, for his work with risk management.

Choppy says when managing risk he uses the tools supplied to him by Wilson Bros. It's a simple and easy to follow matrix that follows a standard format with coloured groupings – high risk (red), acceptable risk (yellow) and low risk (green).

Choppy has become adept at using the risk matrix as a tool to assess his work and as a guide for important communication. He says, "if you can measure something you are more able to communicate about it accurately, and pass on what you need to do to bring the risk level to acceptable. In my job I need to be able to identify what is high risk and what is required to make things safe. Communication is a big factor when you are in a high-risk situation. That's when you know straight away what's required and who needs to be involved."

Some of the situations he gets into are "mind boggling" and that's when he uses the risk matrix system exactly as it was intended. He says that success comes when he steps back and takes some time to assess the risk. In his words: "There are times when you have to step away, make a cup of tea, have two cups of tea – before moving ahead with a new plan."

Choppy is well respected and known for paying close attention to what is happening in the wider forest environment and to the people working in it. He once spotted some tree fellers working as the wind was coming up, he called the harvesting crew to tell the foreman that the tree fellers were working in a high-risk situation. This achieved the right response, and the workers were removed from that situation.

On another occasion, he assisted a harvesting crew out of a tight spot when they needed to move their hauler up the hill to a new position. This was on a steep section of a track he was building with unstable batters. The crew was impressed at how Choppy used his risk management process to ensure the job was made safe. Because of the risk he asked for an observer in radio contact. The observers job was to immediately alert Choppy to any earth movement that could compromise the safety of the operation.

Choppy mostly works on the lands he is affiliated with such as the Tūhoe forests. When talking with Choppy it's very clear that he has great respect for his environment and people. His local knowledge helps when identifying those that have gone before him and preserving the history and mana of the area.

"Respect the land you are working on – other people have been there before you! Step carefully round a Pa site – don't do anything wrong on the land."

While the land may now be covered in trees, communities once thrived in these hills. The combination of his local knowledge and physical identifiers enables sites to be preserved. Choppy adds: “It takes good planning and earthworks to ensure the ground is preserved. Earthworks around a Pa site need to be minimised or another route taken rather than just cutting into the hill.”



A Pa site (pictured in the scrub above the road) that was worked around (not compromised) by altering the planned engineering works.

When starting work in a new forest Choppy will take time to say a karakia. “Safety and looking after the environment is not just a physical thing. If you go in to a job without consideration of all the factors it’s going to end up with a rough job which is no good to anyone.”

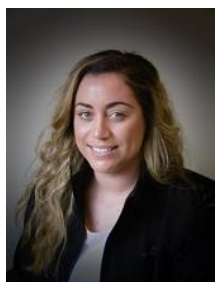
Choppy grew up in this rural setting, and went to school locally. At every chance he’d get on his horse and take off for the hills. His passion now is another type of horse power, as he and his granddaughters are into V8 racing cars. He is also a volunteer planting native species around streams to restore the environment. These efforts are commendable and along with his work in safety made him a worthy recipient of the 2016 Safety Champion’s Award.

Well done! Keep up the great work Choppy!

New staff



Boon Tan returns to the sunny shores of NZ after more than 4 years working on secondment to MPI, working with PF Olsen Australia, and enjoying an OE with his partner. Boon joins the Forest Management team in Rotorua.



Amy Adler commenced in Rotorua 18th September. Amy is part-time Reception/Admin and Training Coordinator.