P.O. Box 602, Blenheim 7240, New Zealand Phone 03 578 1733 Website: www.marlboroughforestry.org.nz
Fax 03 578 1797 Email: info@marlboroughforestry.org.nz

December 2011 Newsletter

Treetop Views

Hi Everyone,

This is my first view from the treetops as your new president. It is a very interesting time for Marlborough Forest Industry Association members. Most of those who planted before 1990 have either harvested their first crop, or are planning to do so. There have been some good prices paid for logs over the last 2 years. With record export volumes, the Marlborough forest industry has been thriving at a time of world recession and while some other sectors of the Marlborough economy have been suffering.

The AGM in October featured two exciting forestry developments, biochar, and the new cross laminated timber or Xlam plant coming to Nelson. You can see more details in the AGM report below and at www.xlam.co.nz. Since the AGM your executive committee have been discussing ways to highlight the many positive aspects of Marlborough Forestry. We have adopted an old Forest Service theme "**Growing Trees for Profit and Pleasure**" and we have a more dynamic committee structure with leaders for 17 different aspects of forestry.

One important aspect is Using Marlborough Wood. Congratulations to Glenroy Housing for winning the supreme house of the year at the Registered Master Builders finals in Auckland. This house was built mostly of wood and was prefabricated and finished to a very high standard in Glenroy's factory near Blenheim.

This house recently featured in the Marlborough Express which you can see at http://www.stuff.co.nz/marlborough-express/news/6003059/Top-gong-for-wee-beauty

The house features Tasmanian blackwood flooring with pine poles, framing, board and batten plus mdf prefinished wall and ceiling panels. It is great to see our pine going into high quality houses such as this, rather than just being used for concrete boxing. Wood seems to be featuring in many award winning architectural and housing competitions. Wood is coming back into fashion which is great for the future of our industry.

When you receive this newsletter, I will be in Germany at the International Wood Building Conference where 1400 people will hear of the latest developments in using wood for houses, supermarkets, shopping malls, bridges, etc. After last year's conference I was shown through a factory near Munich where the world's largest wood structure was being prefabricated out of LVL. The components were then transported 2,300 kms to Seville in the south of Spain. The completed building protects Roman ruins and has walkways to give great views of the city. For more pictures of this amazing building see http://www.kuriositas.com/2011/05/metropol-parasol-largest-wooden.html

All this wood development in central Europe is putting pressure on wood supplies which is great for the local forest owners. Logs delivered to the sawmill peaked at over !00 euro per cubic metre, or $NZ175. Wood buildings are still very competitive because of the high levels of automation and prefabrication in factories. New Zealand is trying to catch up with the Europeans and PrefabNZ has been formed to improve the quality and productivity of the building sector. See www.prefabnz.co.nz. They are setting up an innovation park at the Christchurch Showgrounds to be opened next March. Watch this space.

Our forest industry association is unique in that it represents a good mix of corporate, individual and family forest growers, as well as associated services. We now have over 170 members and we are welcoming new members such as corporate forest owner Ernslaw www.ernslaw.co.nz, Lee Paterson of Pinoli pine nuts www.pinoli.co.nz, and well known forestry consultant Allan Laurie www.laurieforestry.co.nz.

There are many interesting aspects to our organization and what we do. Our forests range from Durville Island down to the Clarence Valley and include many idyllic settings in the Sounds and Marlborough valleys. Some of our forests were planted on some of Marlborough's steepest hills because of their environmental benefits, including their ability to stabilize eroding hillsides and to reduce flood flows.

One of Marlborough Forestry's strengths is a very high labour productivity. A 5 year survey of Marlborough's 6 main primary industries showed that forestry's added GDP per full time employee was about double the rest. Why is forestry so productive? New mechanized harvesting systems, heavier log truck weight limits, and trees being planted for both wood and carbon storage will increase this productivity even further. Productivity gains from automation and prefabrication in the building industry will further increase forestry's value to the Marlborough economy.

High productivity is needed for a strong local economy. The recent election campaigns showed that there was also a strong interest in creating green jobs. What could be greener that planting trees and using wood. This little youtube video from Denmark will appeal to the younger generation, and the young at heart. Can wood solve all the world's problems? http://www.youtube.com/watch?v=WRwA291NAuM&feature=youtu.be

You will see from the committee structure that we plan to cover a wide range of subjects related to the forest industry. Look forward to some interesting field days and newsletters next year.

Enjoy the festive season and may the New Year bring you more profit and pleasure.
Regards
Michael Cambridge (President MFIA)

MARKET UPDATE
December 2011

Export prices and demand are firming up after a difficult few months. Prices followed the expected downwards trend during our winter as China demand for pine softened during their wet season. In September stocks began to fall and prices rose as construction activity appeared to improve, again following expected trends. However this proved to be short lived and prices slumped in October surprising many exporters.

The basic reason for the downwards price movement in October was due to a significant supply/demand imbalance in China. Record volumes of logs and lumber from New Zealand and the Pacific North West (PNW) flooded into China on top of already high stocks resulting from the wet season. Consumption couldn't keep pace and stocks swelled to 4 million m3. Inevitably this resulted in downwards price pressure that sent exporters scrambling. Korea, India, and SE Asia all followed the price trend as volume was diverted from China to these markets.

An increase in prices and reduction in stocks in September gave many exporters false hope. In reality the issues affecting demand and consumption in China went far deeper. For some time the Chinese central government has been tightening availability of credit in the economy in an attempt to cool a red hot property market and control inflation. Businesses couldn't obtain credit to purchase raw materials, construction slowed and this ultimately effected demand for logs. Record log imports in October finally broke the camel's back.

In New Zealand falling freight and a weaker FX meant that prices have remained quite reasonable. Production didn't slow to any great extent and business continued more or less as usual. But the PNW has more than halved production and has low stocks in the supply chain. Russia has also slowed log exports as it struggles with lower Chinese prices.

At the start of December China's central bank surprised markets by cutting the reserve ratio for commercial lenders by 50 basis points. This reduces the amount of cash banks need to hold and increases the amount they can lend. It's the first time China has done this for 3 years and the move is aimed at boosting liquidity in the economy.

As a result there's already been a small lift in sawmill activity in China and prices have started to lift. Aided by lower imports from the PNW and Russia log stocks are starting to reduce. A slowdown in NZ exports over the Xmas holiday period will allow China a chance to reduce stocks further.

The outlook for the first part of 2012 remains as uncertain as always. While there are some positive signs, Chinese New Year is fast approaching in January so we don't expect a great deal of price movement until after that. As the market improves the PNW will increase log exports again and competition will increase. And as exports increase freight costs will also rise. Then there's the debt crisis in Europe and what will happen there is anyone's guess. However the present outlook remains relatively positive and we expect export prices to improve slowly. Korea and India will follow China's lead.

There's no real change in the domestic market outlook. The industry is still battling difficult conditions due to high log purchasing costs, a high and wildly fluctuating FX, and poor market demand. House starts in NZ and Australia remain at record lows, competition in China and the US is intense. Demand in Nelson and Marlborough is likely to remain steady but if conditions don't start improving there could be pressure on domestic prices next year.

Brendon Whitley
Nelson Forests

Growing Trees for Profit and Pleasure

The committee would like to welcome Michael Cambridge as the new President of the MFIA. We would also like to thank our previous president Kevin Parkes for the hard work and great contribution he brought to the MFIA during his term. With Michael's appointment we also have a revised committee structure as below, keep an eye open for new developments next year.

We would also like to welcome three new committee members;
Mike Gifford: Owner/manager of CRB Transport, specialising in log cartage.
John Horton: Operations manager for Nelson Forests Ltd Marlborough team, based at Kaituna.
Vern Harris: Vern has been helping out the MFIA for some time and we've finally persuaded him to officially join the committee.
All three bring some excellent forest industry experience into the organisation.

	Committee	Leader	Purpose
1	Field Trips & Seminars	Michael Cambridge	Work with committee leaders to increase range of interesting field trips and seminars
2	Newsletter & Website	Brendon Whitley	Collect interesting news items from committee leaders for regular newsletters
3	Environment & Regulatory	Rick Osborne	Highlight the environmental benefits of forestry and look for opportunities for improvement.
4	Markets, Carbon Trading & New Planting	Aaron Robinson	Report on markets for wood and carbon. Highlight and encourage new planting.
5	Fire, Safety & Training	Vern Harris	Report on new fire regime.
6	New Developments & Innovation	Rick Osborne	Highlight and research projects such as biochar, CLT or Xlam, and wood chipping.
7	Harvesting, Roading & Port	Kevin Parkes	Highlight harvesting innovation, heavier truck loading, block owners sharing roads and skids.
8	Forestry for Recreation	Murray Turbitt	Mountain biking, tramping, 4WD, and hunting opportunities for members and public. Highlight good relationships with recreational users.
9	Forestry as a Career & Forestry for the Next Generation	John MacKenzie	Profile people working in forestry. Encourage next generation to grow trees for profit and pleasure.
10	Bioenergy	Mike Gifford	Existing and future uses of wood for energy.
11	Upcoming Events & links to other organisations	Ron Sutherland	Marlborough Chamber of Commerce, NZFOA, NZ Farm Forestry, and Marlborough Research Centre share our interests
12	Early days of Marlborough Forestry	Ron Sutherland	Learn from the past. Profile people involved in setting up the Marlborough forest industry.
13	Second Crop	John Horton	Second crop pine trees grow much better than the first, but what about options, Redwood, Eucalypt, Douglas Fir, Cedar, or return to Indigenous?
14	Measuring Carbon	Aaron Robinson	Members with over 100 hectares of ETS forest will be measuring their carbon next year.
15	Using Marlborough Wood	George Shallcrass	Highlight and encourage the use of Marlborough grown wood of all species.
16	Membership	Tamati Smith	Profile members and their forests, and encourage new members.
17	Odd Stuff	All	Quirky and fun stuff related to the wood industry.

CARBON MARKETS

With international Kyoto negotiations taking place for the next commitment period this subject is very topical at present. Following we have two informative articles on the carbon market, one from Rick Osborne and one from Aaron Robinson.

CARBON CREDITS – WHERE TO FROM HERE?

Currently "carbon" is the worst performing commodity in the world. The NZU price which has hung at around $20 until mid.2011 is now $10. Europe seems to be awash with carbon credits as their industry slows and an ever increasing supply of credits is generated. NZ emitters are allowed to purchase and surrender these cheaper European units to meet their obligations and it is they that drive the price of NZUs. Adding irony to the situation is our high NZ dollar which makes these European units even better buying for NZ emitters.

It is a difficult decision to hold or to sell credits at the moment and I suspect that most foresters will choose to hold rather than sell at present levels. The decisions made will depend on personal views and circumstances and rather than recommend anything I will tell what I am doing and my reasoning.

At this stage I have sold approx. half of the credits that we hold for between $20 and $11. I am in a holding pattern at the moment, mostly holding my breath and hoping that the price slide does not continue. But why should it not continue to say $5? There is no underlying cost of production for a carbon credit, some sellers could keep selling down to 1 cent and still they would be better off than at zero. Carbon credits have a price but they don't have a value.

I am quite "long" carbon, in market parlance, I have more of it coming along each year, I am getting a bit long in the tooth myself so why not cash up and enjoy. I can use the money for projects that are worthwhile. It is a lot more fun doing things than looking at a number in the Emissions Unit Registry.

There has been talk that the NZ Government could move to restrict or ban the use of European CERs by emitters to meet their obligations. I don't think that will happen. The

Government needed to soften the effect of the ETS on our economy and exporters with the $25 price cap and the 1 for 2 deal until Dec.2012. This has partly turned our ETS into a "Claytons" ETS, but we can still look like "greenie two shoes" on world trade and political stages. In addition, it looks ever less likely that the ETS will be applied to agriculture. Right now the market is doing the NZ Government's softening job for them, why would they want to underpin the price?

We have the overhang of pre 1990 "Allocation" credits to add to supply over the next three years.

My pick is that the price of NZUs will stay low for the next two years or more. I think that there is a fair chance that a credit sold now can be re-purchased for similar or maybe even better price later on – if you want, or need, to do that of course.

In the fullness of time, you can laugh at me, or you will say I was wise.

The graph below from O M Financial shows the NZU price history and if you want to check carbon pricing you can access live NZU pricing on www.commtrade.co.nz. OMF also email an excellent weekly report. If you are interested in receiving it please contact Nigel Brunel – nigel.brunel@omf.co.nz, with your email address.

Rick Osborne

THE NEW ZEALAND CARBON MARKET

Over the past six months the world carbon markets have been in free fall. Since March this year the spot rate for the New Zealand Unit *(NZU)* has dropped from around NZ$21 to the current rate of NZ$7.80.

The erosion of the carbon price has adversely affected what the NZETS set out to do – to reduce greenhouse gas emissions. If the current, low carbon prices continue there will be no incentive for emitting industries to reduce emissions or for investors to support carbon forestry projects. It is likely that the area of commercial forestry in New Zealand will decrease with penalties for deforesting Pre-1990 land quickly evaporating. Eight months ago the emission liability for deforesting Pre-1990 land was around $17,000 per hectare as compared to a liability now of around $6,200.

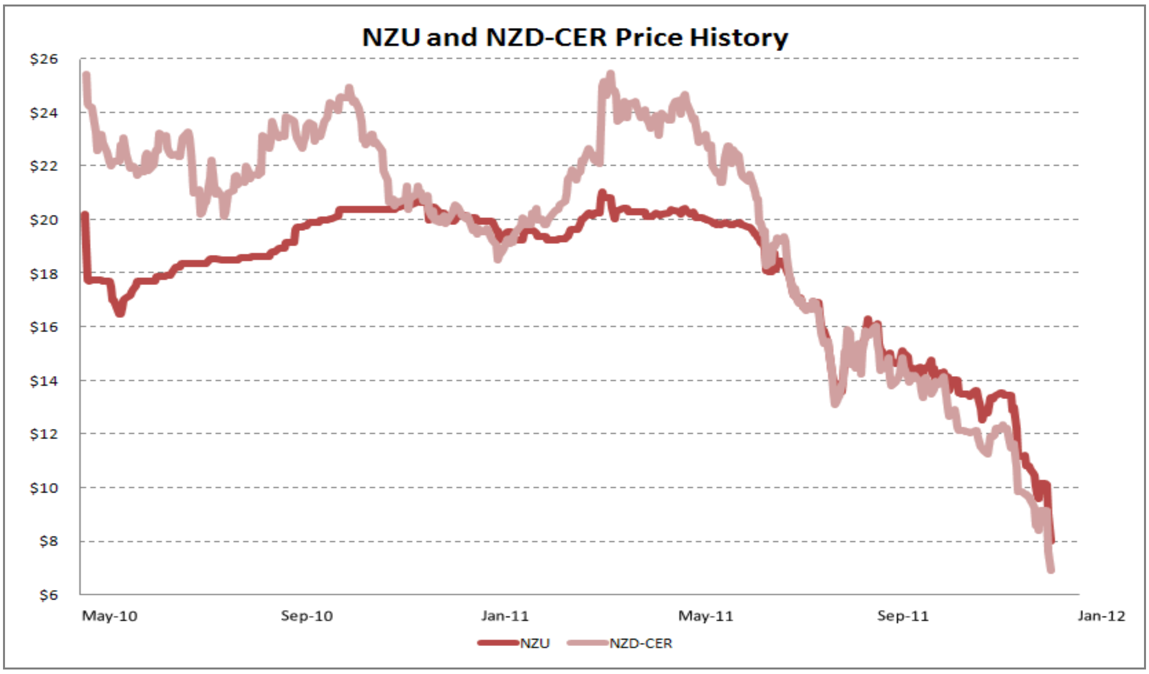
What has caused the carbon price to fall?

New Zealand emitting industries can purchase domestic forestry carbon units to cover liabilities. In New Zealand these units are NZUs and Assigned Amount Units *(AAUs)*. New Zealand emitters can also purchase carbon units from Europe, Certified Emissions Reductions Units *(CERs)*, to cover liabilities. Until recent months, CERs have almost always commanded a premium price over NZUs.

During 2009 and 2010 when the New Zealand carbon market had less liquidity than now, brokers often used a guide for the price of NZUs at around 80 percent of CERs.

The NZETS appeared to be working well once emitters started entering the scheme. There were incentives for investment in forestry carbon projects and for emitters to reduce emissions. New Zealand and some European emitters purchased NZUs and AAUs (domestic units) due to the discounted value over CERs (European units).

Then the European economic crisis hit this year. Due to the slowdown of industry in Europe, cash strapped businesses have been selling excess CERs to improve balance sheets. In Europe the supply is expected to outstrip demand. Deutsche Bank considers that this will continue until at least 2020. As a consequence, there has been a sharp decline in the European carbon price. This has played into the hands of the New Zealand emitters: why would they pay $20 for an NZU when they can cover their liabilities with CERs at a current price of around $8? The NZU and NZD-CER Price History graph below shows the price of the NZU and CER (adjusted to New Zealand dollars) over the past eighteen months. It demonstrates that the value relationship between the NZU and CER has reversed, with the NZU now being about $1 more expensive than the CER.



Source: ***Westpac Banking Corporation***

Many New Zealand forest owners have been waiting for the NZU price to come back to the $18-$20 per unit mark before selling. It may be some time before the NZU gets back to the $20 mark with many NZUs currently sitting in New Zealand *Holding Accounts*, many Pre-1990 NZUs still to be transferred, a new round of *Emissions Returns* to be filed for Post-1989 Participants and many emitters having purchased CERs to meet upcoming liabilities. Just like Europe, it appears that supply of NZUs will be greater than demand for some time.

Will the Carbon Markets Improve?

Although the market is doom and gloom at the moment there is some light at the end of the tunnel. An Independent Review Panel *(the Panel)* released its findings on the NZETS on 15 September. The information released by the Panel contains recommendations for the Government to consider. Recommended changes from the Panel which may improve the market are:

- Transition Mechanism: Current emitters only have to cover 50% of their liabilities. This is proposed to be phased out to full surrender by 2015 (67% in 2013, 83% in 2014, 100% in 2015)
- Unit Coverage: For Government to give urgent consideration to whether Industrial Gas CERs should be excluded. Industrial Gas CERs have low environmental integrity
- International Linkage: Emphasis on strong linkages with international schemes going forward, including Australia and EU
- Agriculture: No delay recommended. Agriculture obligations to commence (as per current legislation) in 2015

Some positive themes have emerged from the recent international climate change negotiations in Durban. Political leaders agreed to extend the Kyoto Protocol, with the second commitment period beginning in January 2013.

Carbon demand in New Zealand should improve with synthetic gases and waste joining the NZETS in 2013. Agriculture will join in 2015.

Summary

The oversupply of carbon and a weak economic global outlook are the two fundamental problems with the current market. Until, in particular, the European economy improves and/or limits occur on CERs the New Zealand carbon market will not improve.

At the current carbon price level the NZETS will not achieve what it was designed to do. There is no incentive for emitting industries to make reductions and to invest in new forests.

These low prices have created an opportunity for Post-1989 Participants who have sold units at values often much greater than today's price. Why not pull out of the scheme by buying back units they have sold. By doing so they would have made a profit and have no liabilities for any decrease in carbon stock at harvest time. This may be an attractive opportunity for those who have greater than 100 hectares and have the cost of the *Field Measurement Approach* coming up before the end of 2012. These forest owners can always re-enter the scheme later.

Aaron Robinson (19 December)

The MFIA committee would like to wish all members
a great and safe Xmas and happy new year.