Forestry Tasmania, Market Trends and Financials

Graeme Wells

School of Economics and Finance

University of Tasmania

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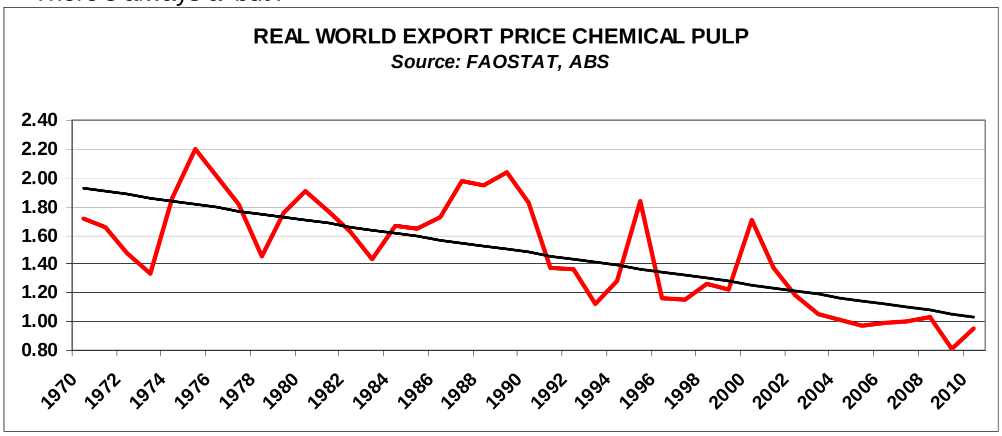
Undifferentiated Products?

Not necessarily losers – e.g. iron ore, coal

There's always a 'but'!



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Many have argued that it's a poor economic strategy to focus on production of undifferentiated primary products. Try telling that to Gina Rinehart, Andrew Forrest and Clive Palmer. The more important issue for profitability is the long-run trend in prices. If prices are falling, it might be wise to think about alternative strategies. The chart above shows the world price of chemical pulp, expressed in real Australian dollars. It's hard to argue that so-called eco terrorists have had any impact on this price series. The price trend is not a pretty picture.

Market trends

- Price of structural grade timber – down 5% in real terms, 1990-2011. (URS Report p.38 and Australian Bureau of Statistics)
- Real World export price of chemical pulp – down nearly 50 % in real terms 1970-2010 (FAOStat and Australian Bureau of Statistics)
- Real export price of native forest woodchips: falling in Japan and likely to remain lower in China (URS p.32)
- Response: Reduce input costs, produce more sophisticated products from low cost feedstocks – e.g. manufactured lumber products.
- Forestry Tasmania response? Ta Ann and not much else.

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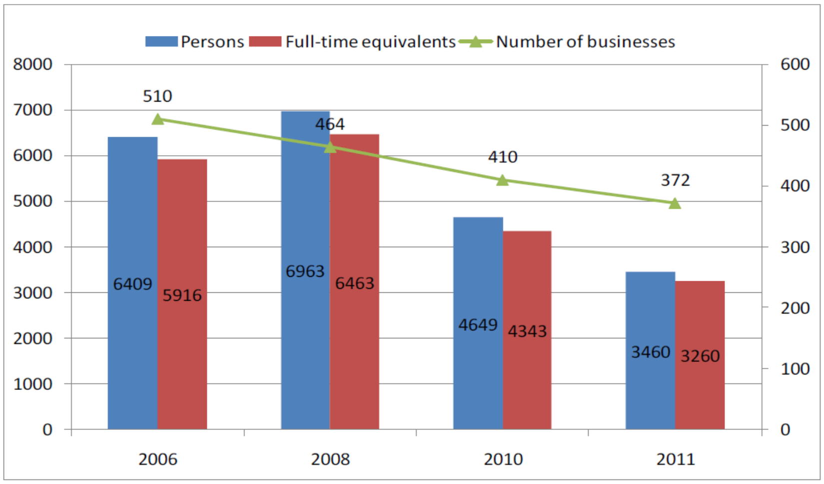
Price trends shown on the previous slide are also reflected in native wood products generally. A normal commercial response would be to reduce input costs and upgrade technical capacity to value-add low cost feedstocks into a range of manufactured timber products. This is precisely what a whole range of reports have called for over the last decade, (Australian Conservation Foundation and Wilderness Society 2004, various editions of the Greens Forest Transitions policy 2002, 2004, 2010, Australian Innovation Research Centre 2009, FFIC 2010).

The only significant response by Forestry Tasmania has been to promote Ta Ann's use of peeler billets. While this is better than chipping trees, a whole range of other options have not been explored in any depth. The annual GBE hearings into Forestry Tasmania sometimes are sometimes entertained with thought bubbles (last time some tee shirts, made from wood pulp were pulled out of the bag) but it is difficult to see that FT has had the incentive or the inclination to aggressively explore alternatives.

Employment Trends (Schirmer 2011)



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In 2006, forestry (broadly defined) employed 2.8% of the Tasmanian workforce. Today (2012) the proportion is estimated to be less than 1.2%.

Employment trends reflect declining profitability. Today there are probably less than 3000 people employed in the industry, defined to include harvesting, processing, transport, FT, consultants etc. Not all these jobs (the Norske Skog mill, for instance) are at risk from the IGA process. Claims as to the present importance of the industry to the Tasmanian economy tend to be overstated, although the consequences for individual forestry families are severe.

Forestry Tasmania financial performance

- Average return on assets 1995-2010: 1.84% (p.63) *Auditor General (2011)* 1995-2012: 1.7%?
- 'Based on current levels of cash flow, Forestry will find it difficult to fund its defined benefit obligations' *Auditor General (2011)*(p.3)
- 'If Forestry wishes to continue with its current level of investment in plantation development sources of government or other funding of approximately $200m to $250m will be needed' *Auditor General (2011)*(p.5)

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There is a variety of ways in which FT financial performance can be assessed (e.g. Naomi Edwards' comparison with SA forestry) but my preferred measure is the rate of return on assets. On the Auditor General's approach (which makes very generous allowance for community service obligations etc) the target should be 2-3%. FT fails to meet even this target, and is presently in need of cash injections to keep it going in its current form.

Forestry and Gunns

- Forestry adopted the strategy advocated by the Pulp Mill Task Force, aligning its corporate strategy to its major potential customer.
- With the collapse of tax-driven MIS schemes, a sequence of poor investment decisions, and the likelihood that electricity generated from native forest biomass would not be eligible for Renewable Energy Certificates, the major customer (Gunns) exited and this strategy collapsed.
- Question: Would this strategy have been adopted by a Forestry Tasmania more independent of government policy? Or is a fundamental restructure required?

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Following CEO Mr Gordon's return from a stint on the Pulp Mill Task Force, FT and the government were in lockstep on the strategy of getting the pulp mill up. In this environment it is not clear that a greater degree of government oversight would have improved FT outcomes. The major parties were cheering FT on.

When Gunns exited native forestry, receiving ample compensation despite the fact that their wood supply contracts could have been terminated with the failure to start operating the pulp mill, FT's failure to undertake feasibility studies on alternative processing options (LVL and other manufactured wood products) really started to bite.

Questions to consider. Would an FT given more independence have managed risks more effectively? Would it have been better at identifying alternative processing options? Do management of conservation values and maximising the potential of the Tasmanian forest industry require two separate organisational structures? How would they differ?