

Report to:	Council	File PUBLIC EXCLUDED
Date:	29 March 2023	
Subject:	Marlborough Regional Forestry Land Acquisition	
Prepared by:	S Poulsen - Finance Manager	
Input sought from:	M Fletcher - Chief Financial Officer, Marlborough District Council	
Authorised by:	W Doughty - Chief Executive	

1. SUMMARY

This report seeks Council's approval for the purchase by the Marlborough Regional Forestry joint venture (MRF) of 178 hectares of greenfield forestry development at 3346 State Highway 6, which is just before Twidles and Prices Roads on the way to Havelock, Marlborough.

Attachments:

1. MRF – Investment Guidelines
2. Valuation Report (Colliers)

The attachments are for information only.

2. RECOMMENDATION

THAT the Council:

- a) Receives this report, and
- b) Agrees to the purchase by the Marlborough Regional Forestry joint venture of 3346 State Highway 6, for \$2.05 million plus GST (if any).

3. BACKGROUND

Over recent years, MRF has been looking for forestry blocks that make good economic sense, particularly those that will fill the harvest gaps identified to occur when there are no trees at suitable maturity for logging.

Marlborough Regional Forestry (MRF) became aware of a block at 3346 State Highway 6 coming to market, with a deadline sale date of 1 March 2023. The property is a 178-hectare (subject to survey) moderate to steep hill country property which is currently used as a sheep and beef pastoral farm.

The property offers a greenfield development with approximately 160 hectares of land suitable for Pinus Radiata plantation and registration into the ETS as Post-1989 land, additionally 15.19 hectares of land has been identified as potentially suitable for indigenous ETS registration over time and the remaining 2.81 hectares has previously had a pre-1990 tree crop in a number of small woodlots that have been harvested. Improvements are limited to an airstrip and fertiliser bin.

Access to the subject property is via a proposed Right of Way from State Highway 6 on completion of the proposed subdivision. Fencing and tracks are of a good standard. The property is located within a desirable forestry growing area having high rainfall, low altitude and easy access to ports and mills.



Previously one of the challenges of purchasing forestry blocks has been the closing dates for tenders and the timing of the Council approval process. Clause 32(1)(c) of Schedule 7 of the Local Government Act 2002 states that a local authority may not delegate “(c) the power to borrow money, or purchase or dispose of assets other than in accordance with the Long-Term Plan (LTP)”.

To address this situation a paper was presented to the Council’s 31 August 2022 meeting. That paper gave the two Chief Executives (of Marlborough and Kaikōura District Councils) the power to make an offer, subject to final Council approval and the target land meeting certain investment criteria. The investment criteria is attached to this report.

M&R Forestland Management Ltd and Megan McKendry (MRF’s independent committee member) have completed an assessment of the forestry block against the MRF investment criteria, and their combined findings are as follows:

MRF Investment Guidelines

a) Size

3346 SH6 forest is approximately 160 hectares and meets the guidelines of size (minimum of 100ha beyond 10km of estate).

The size of 3346 SH6 will achieve economies of scale, will provide at least two years of continuous harvesting, and is large enough to ensure efficiencies with day-to-day tree crop and estate management.

b) Forest Location

3346 SH6 is located within the Marlborough District. It is not within coastal zones or afforestation flow sensitive areas. It therefore meets the location guidelines.

c) Age Class

The 3346 SH6 is bare land, which will be planted in 2024.

Other Benefits

The 3346 SH6 forest will fill part of the gap in the age profile of the MRF forest estate. Currently there is a four-year harvest gap. This means that there is a four-year gap right throughout the growth period, which has negative impacts on cash flows and the retention of workforce. 3346 SH6 forest will fill at least 2 years of this gap.

This property provides a good opportunity to purchase bare land that is in a very good location, good size and has potential ETS benefits. M&R have the expertise and labour available to carry out land preparation, planting, and release works on this property.

Other Questions asked with answers as part of MRF's due diligence on whether to make an offer included:

a) What is the potential for future slash issues to arise?

The main slash issue now is on the East Coast where they have very young fragile soils and significant areas of first rotation forests have been harvested in recent times. I think there will be some change in land use or accepted practices in that area however I do not think there will be significant changes here in Marlborough over and above what we are currently doing.

For good quality forestry land in Marlborough whether it is bare land, cutover or already planted I do not think land values will change significantly due to slash issues we are currently seeing in the media. Any change in land value will be driven by log & carbon prices.

Any blocks that are discounted will probably be high risk and they would not meet our investment criteria.

b) As a high rainfall area, in the event of a significant weather event resulting in severe erosion, slippage, is there the possibility of mud and slash hitting SH6?

In the event of a debris flow, the runoff is at least 600m to SH63, so it will not have the momentum to reach the highway. The benefit of this property is the amount of rock in the soil, which adds to the stability of the site. Environmentally this site has higher soil stability than the MRF forests in Speeds and Koromiko. Slash management practices and construction techniques have improved, which will decrease future risk.

c) There is a ROW to be created (LIM report says it is Limited Access Road) on Subdivision being approved. Does the proposed road provide good access for harvest in the future?

The proposed road provides direct access to the property, the property subdivision will be subject to parties agreeing where the final survey boundaries are located, this will ensure that the formed track along the bottom of the hill will be included in the Subdivision – when driving along the track this is fenced and makes a logical boundary from the farmed flats.

d) LIM mentions a drain on the property – is this a potential issue for setbacks? Roding?

For roading purposes, any setbacks from waterways needs to be a minimum of 10m, other than when installing a crossing, so we would treat this like all other streams we manage, currently there is a ford crossing, so at time of harvest time the management of these crossing will be an improvement on farming practices. In terms of afforestation then are several intermittent and / or Ephemeral streams on the property and we would afforest the property with appropriate setbacks.

e) Plugging the 4-year harvest gap, with the Sunhill Block as well as this block, is the hole filled? Another 2 years would be ideal; however the purchase of this property will leave MRF in a better position to smooth the future harvesting operations.

- f) Because of public visibility of this location under MRF ownership is there the potential of keeping the block environmentally secure, with a mix of plantings exotic and native with any wetland areas?

I have checked the MDC Maps and there are no significant wetlands present on the property. Gullies have native present, or are in the process of reverting, so am confident that in time Manuka and kanuka will establish once stock is removed. Established natives in gullies will give greater protection at time of harvest.

- g) Based on the Colliers pricing is there strong demand currently by other parties seeking forestry investments - where is the market at locally, are we competing?

Yes, this has generated interest and there will be a multi offer made on the property.

Following the completion of MRF's due diligence and the obtaining of valuation report from Colliers (Attachment 3), it requested that Council's Chief Executive make an offer of \$2.05M. This offer has been accepted subject to Council approval.

Is \$2.05M a reasonable price to pay?

A valuation was prepared by Tim Gifford of Colliers. The Executive Summary is contained in Attachment 2, with the full report available on request. The valuation arrived at a value of \$1.96M. However, as it was known that there were 4-5 other parties seriously looking at the block including at least two overseas investors, an increased figure of \$2.05M (+4.5%) was offered. We note this is within the Council's agreed limit of no more than 5% above valuation.

Note the Government's 2018 Special Forestry Test and the Overseas Investment Office's exemptions for forestry rights of < 1,000 hectares in a year has made forestry one of the easier classes of investment. The block is also a good size for larger family trust investments. Should both Council's approve the purchase, settlement will take place once title is granted, indicatively around November 2023.

Two other points to note are:

- a) that approximately 65,000 emission trading units will accrue on the block and at today's price of \$65.25 this equates to \$4,241,250; and
- b) It helps balance Council's Carbon footprint.

Funding

Funding will be sourced from the sale of MRF pre-1990 carbon credits. There will be no impact on either rates or debt.

4. FINANCIAL IMPLICATIONS AND RISKS

The outcome of the land purchase is that MRF has expanded its asset holdings by purchasing an ideal forestry block with second rotation trees and has filled a harvesting gap that alleviates future phases of cash losses.

As noted above, there are sufficient carbon credits held by MRF to fund the acquisition without any draw on rates, debt or reserves.

4.1 Community Implications

There are no implications to the communities in either Kaikōura or Marlborough districts.

4.2 Risk Management

There are no known risks identified with this land purchase.

4.3 Health and Safety

There are no implications to health and safety in this report.

5. RELEVANT LEGISLATION

5.1 Policy

The Council's Financial Strategy is for forestry to generate cash surpluses after having covered all associated costs. The expansion of MRF's holdings to now include 3346SHN6 and the recently purchased Sunhill block will ensure there are few (if any) periods of cash losses in the future, due to the maturity of the trees filling the current harvesting gap.

5.2 Legislation (Local Government Act, Schedule 7, Clause 32 (1))

By ensuring the Council approves the land purchase, this acquisition complies with the Local Government Act.

5.3 Community Outcomes Supported

The work is in support of the following community outcomes.



Future

We work with our community and our partners to create a better place for future generations



Development

We promote and support the development of our economy

5.4 Delegations

As discussed in this report, only the Council has the power to purchase or dispose of assets and this power cannot be delegated. In this instance, for the MRF joint venture, the power needs to be exercised by both the Kaikōura and Marlborough District Councils.

6. COMMUNITY VIEWS

6.1 Groups and Organisations

The matter is not considered to be an item appropriate for engagement with any groups.

6.2 Wider Community

No community views have been sought.

ATTACHMENT 1: MRF INVESTMENT GUIDELINES

Marlborough Regional Forestry – Land Purchase

The purpose of this brief is to provide a guideline for the most suitable type of property to purchase in order for Marlborough Regional Forestry (MRF) to grow their Estate.

Area

In order to achieve economies of scale, recommendations of the most suitable size of the land are as follows:

1. Minimum of 100ha beyond 10km of estate

A 100ha block will provide one years' worth of continuous harvesting and the size is large enough to ensure efficiencies with day-to-day tree crop and estate management.

2. 50ha within 10km of current estate

A 50ha block near the current estate will provide six months of continuous harvest and due to the proximity of the current estate, day to day tree crop and estate management can still be managed efficiently.

Forest Locations

To simplify the process of selecting a suitable forest block the following locations will not be considered

1. Outside the Marlborough District Council boundary

To ensure no outlier forests, land within the Marlborough District boundary should only be considered.

2. No land with the Marine Coastal Environment (the Sounds) will be considered

While M&R have experience in management of forests within the coastal environment, we also understand the ongoing difficulties of operating within the Sounds and we perceive potential conflict of interest with MDC.

Age class priorities

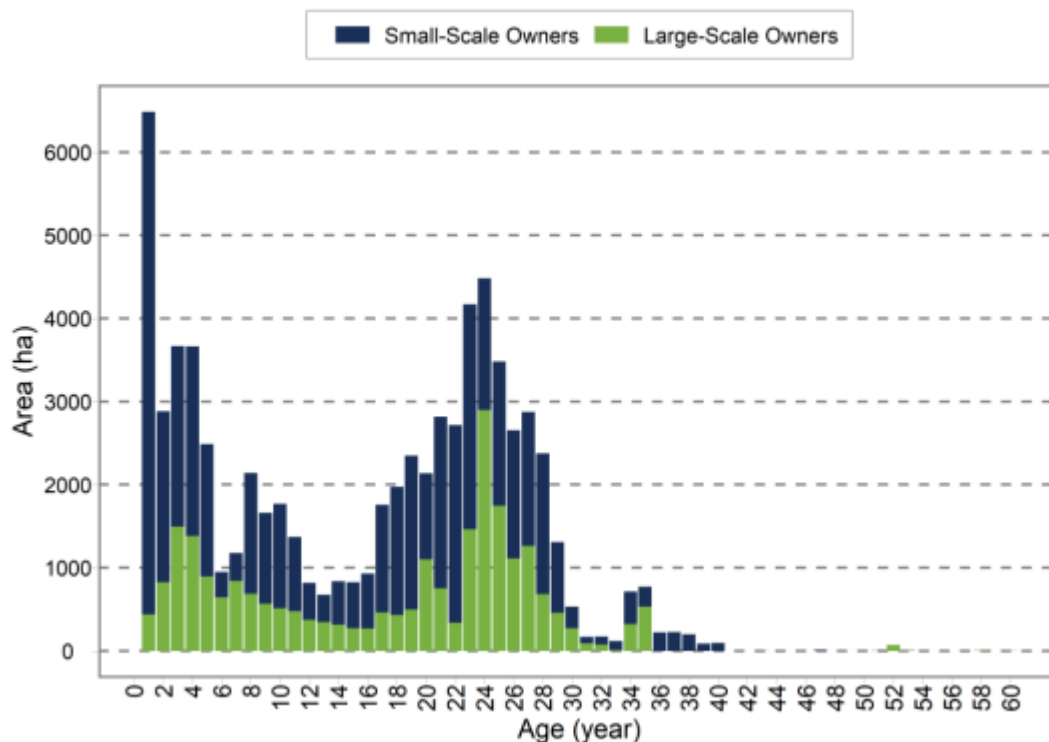
The MRF estate has been harvested at the optimal age, however this has left a six year harvest gap. Additional land or forest purchases will aid in smoothing the harvest to a perpetually sustainable model, the benefit of this has wider ramifications than just consistent harvesting, it will allow MRF to sustain a work force across establishment and silviculture operations, ensuring skilled labour is retained.

Typically, trees that are one-two years old can be valued at the cost of establishment, with this increasing each year. Generally, forests or land with scale that has been entering the market over the last few years has been bare, unplanted or with one – two-year-old trees.

The graph (2021) below shows the age class distribution for forests in Marlborough, M&R are familiar with the structure of forests that are due for harvest. The small-scale owners are either made up of partnerships or held by individuals and are around 100 -200 ha, or they are larger forest areas that have been subdivided into smaller lots and held by individuals, generally around 20 - 40ha.

M&R’s experience is that at the end of partnerships or depending on the age of the individual post-harvest, these are the types of properties which will be offered to the market for sale. As such M&R anticipate younger age classes or cutover coming to the market.

Marlborough Modelled Age-class Distribution for All Species



As a guide M&R recommends the purchase of;

1. Forests aged 1-2 years old

There is no premium attributed to the value of the tree crop, it is second rotation and therefore roads and skids have been built. Recently established forests do pose some risk which is why a premium is not built into the valuation, typically forests established by reputable Forest Management companies have records of quality control, weed control and survival assessments. These can be assessed in the due diligence phase. Other forests may require physical assessments to determine the quality and level of stocking.

2. Cutover land

This is land that has been harvested and is ready to be replanted. The value of the property is in the land, it has roads and skids, but establishing the forest will need to be completed by MRF.

3. Bare land

This is farmland that is suitable for establishing in a forest. Typically, these are low fertility, poor grazing sites. These will be the first rotation and do not have forest infrastructure in place, depending on the farm tracks some engineering may be needed to assist with establishment.

4. Forests age 3-6.

The value for trees starts to increase over time and these forests begin to command a premium for the tree crop. At this age the crop is easily seen and any establishment issues should have been resolved or identified.

5. Age classes 7-15

These forests will either be pre or post thinned stands and command a premium for the crop, depending on the age class and the tending they have received, they may require immediate cash flow for silviculture operations.

6. Age 15 plus

It is less common to see older forests for sale within the region, while these are worth considering, they require due diligence as to their value, particularly those nearing harvest as there is typically competition from log traders in this market.

Carbon

Land valuations consider if a property is eligible for carbon and the land is priced accordingly. Typically, if cutover land is eligible, it will already be entered into the ETS scheme. However, not all bare land meets the criteria and therefore due diligence to determine if it is eligible should be undertaken.

New rules are coming into effect and will apply to all post-89 forests registered from 1 Jan 2023. Forest owners will no longer need to surrender NZUs when they harvest; instead, they receive NZUs up to an average harvest age which for *Pinus radiata* is 16-year-old. The condition is that forests need to be harvested close to target age and replanted. The benefit of this is a reduction in cost and complexity of the ETS for forest owners.

ATTACHMENT 2: VALUATION REPORT (COLLIERS)



Executive Summary

Valuation Details

Instructing Party Kyle Heagney M&R Forestland Management Limited 141 Battys Rd Burleigh Blenheim	Client Reliant Party(s) Purpose of Report Interest Valued Date of Valuation Date of Inspection Date of Report	M&R Forestland Management Limited Marlborough Regional Forestry Market value for potential purchase Freehold 20 February 2023 20 February 2023 27 February 2023
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Property Overview

The subject property is a 178-hectare (subject to survey) moderate to steep hill country property which is currently used as a sheep and beef pastoral farm. We have seen a number of suitable pastoral farms over the past 18 plus months across the country which have been purchased and converted to forestry for logging and carbon farming uses. This has also been evident throughout Marlborough with typical pastoral farmers now having to compete with forestry/carbon farmers for similar hill country, as returns from forestry and carbon farming are now stronger than what is possible from pastoral farming.

The property offers a greenfield development with approximately 160 hectares of land suitable for P, Radiata plantation and registration into the ETS as Post-1989 land, additionally 15.19 hectares of land has been identified as potentially suitable for indigenous ETS registration over time and the remaining 2.81 hectares has previously had a pre 1990 tree crop in a number of small woodlots that have been harvested.

Improvements are limited to an airstrip and fertiliser bin. Access to the subject property is via a proposed Right of Way from State Highway 6 on completion of the proposed subdivision. Fencing and tracks are considered to be of a good standard.

The property is located within a desirable forestry growing area having high rainfall, low altitude and easy access to ports and mills.



Property Data

Address	3346 State Highway 6, Havelock, Marlborough District
Legal Description	Proposed subdivision of Sec 1 Blk XVI Wakamarina SD, Sec 68 & Sec 158 Havelock Subrn Dist, Lot 1 DP 559, Lot 4 DP 1117, Lot 2 DP 12112, Lot 2 DP 395671, Lots 1 & 3 471665
Tenure	Assume freehold estate in fee simple on completion of subdivision
Registered Owner	Dunroon Holdings 2014 Limited
Land Area	178 hectares, subject to survey
Local Government Area	Marlborough District Council
Zoning	Rural 4 Zone

SWOT Analysis

Strengths and Opportunities

- Carbon earning potential
- Medium scale development opportunity of P. Radiata forestry
- Limited non-productive assets on the property
- Aspect and locality
- Farm tracks provide suitable access over block
- Relatively clean and weed free faces
- High rainfall

Weaknesses and Threats

- Volatility in log and carbon pricing
- Complying with rules under the NES for Productive Forestry
- Disjointed shape with Right of Way access
- Registering all potential indigenous forestry within ETS
- Weed and pest pressure when establishing new forest
- Rising interest rates

Special Assumptions

- We assume the proposed subdivision plan will be approved with freehold title issued with no onerous easements or encumbrances noted on the new title, along with Right of Way access from State Highway 6. Should the final area of the subject property differ from the 178 hectares assessed, we reserve the right to reassess this valuation.
- We have assumed that the trees will be registered within the ETS under the averaging accounting method, being harvested at 28 years, and resulting in the income from carbon ceasing at year 16.

Valuation

Valuation Date	20 February 2023
Adopted Market Value	\$1,960,000 (plus GST, if any) One Million, Nine Hundred and Sixty Thousand Dollars

Apportioned as follows:

Land and Carbon Value	\$1,913,000	
Improvements	\$46,000	
Market Value	\$1,959,000	excluding chattels, plant & equipment (plus GST, if any)
Market Value (rounded)	\$1,960,000	

Valuers

Tim Gifford | BCom(Ag) VFM, MPINZ

Registered Valuer

Director | Valuation & Advisory Services

Valuation Review This report has been verified by **Jack Powell | BCom VPM, MPINZ, Colliers | Rural & Agribusiness**

NOTE: This Executive Summary must be read in conjunction with the attached report and the details contained therein.