



MADISON'S TIMBER PREVIEW

PO Box 2486, Vancouver, BC V6B 3W7 ✦ Tel: 604-984-6838 ✦ Email: madrep@shawcable.com ✦ Web: www.madisonsreport.com

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The collapse of a major Australian timber company and sawmill owner this week has sent shock waves through that country's lumber producing industry.

Gunns Ltd was once the largest hardwood sawmill in the Southern Hemisphere, but Tuesday, after more than 100 years of operation, the company fell into administration [receivership - ed]. Gunns' losses are mounting and its bankers have decided they can no longer support its crippling debt levels. More than 600 workers have lost their jobs across four Australian states.

Gunns entered voluntary administration this week, blaming the refusal of its banks to allow it to keep the proceeds of asset sales to keep the company afloat.

Industry watchers are still absorbing the news of Gunns' collapse, after such a long time of dominating Australia's timber business. Gunns has been spreading its roots into a bewildering array of unrelated assets, including hardware stores, wineries and walnut plantations. All are now sold or on the block. Its net assets are stated to be A\$24 million. Just four years ago, this was a A\$1 billion company contemplating a A\$2 billion investment in one of the world's largest pulp mills.

The lenders' decision follows the company's A\$904 million loss after tax last financial year, after write-downs due to the sustained slump in the woodchip export market and lack of investor support for its A\$2.3 billion pulp mill project. As of June 30 this year, the company, which was founded in 1875, had debts of A\$526 million and total liabilities of A\$879 million, almost the same as its total assets of A\$903 million.

Even as the company struggles to settle its accounts, the expected circling of opportunistic sharks has already begun. A number of Chinese buyers are examining Gunns' assets, with Shandong Bohui Paper one of the interested parties for the Bell Bay and Tarpeena sawmills, sources close to the situation said, according to the *Australian Financial Review* Thursday. It is understood there have been high-level discussions in the past week with Shandong Bohui Paper around the two mills, which employ 350 workers and have an enterprise value of about A\$100 million. A heads of agreement [memorandum of understanding - ed] had been signed between the two companies.

Sources close to the industry said Chinese investors were the most likely buyers of not only the timber assets but also any resurrected pulp mill project, says the *Review*. The failed timber company's receiver, KordaMentha, said the pulp mill project might be resurrected under a fresh capital structure.

Keeping the sawmills running and getting the pulp mill project completed and online would be of primary importance to workers and political leaders. To that end, Tasmanian Premier Lara Giddings sought out Asian investors for the beleaguered Gunns pulp mill project during her recent trip in the region. Ms Giddings revealed her pitch on Wednesday as Chinese investors emerged to buy Gunns' assets and even the A\$2.3 billion pulp mill project.

Questions about the viability and future profitability of timber operations remains high on everyone's list, even as dimension lumber prices continue to improve. What is the outlook for timber and log prices, and timberland investment in general?

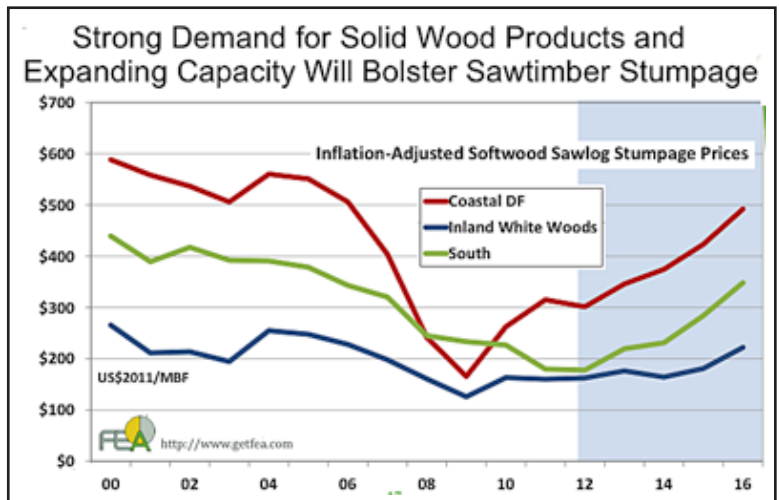
A lot of very good information on these particular topics was offered at the joint Forest Economic Advisors (FEA) and World Forestry Institute (WFI) events last week in Portland, OR.

Vice President of the North American Timber Service at FEA, Rocky Goodnow, in his *'Timber Market Outlook'* said, "It is hard to see a strong recovery in log and timber prices in the next couple of years. West coast US log exports remain strong compared to 2010 but not like 2011. Exports account for 20 per cent of western US log markets."

"Beyond that, there is a significant shift in stumpage prices coming due to changes in Canada," continued Goodnow. "The tightening of softwood sawtimber from north of the border will translate into lower supply. British Columbia and Quebec will be reducing their Annual Allowable Cut (AAC), therefore overall demand in the south and the west of the US will be returning to previous levels."

Presenting in conjunction, Roger Lord of Mason, Bruce & Girard and Jeff Wikle of Terra-Source Valuation spoke, respectively, on US western and eastern *'Timberland Transaction Trends'*.

"Comparing 2011 to 2008, timber harvesting is back in most of the west," explained Lord.



"On the west side, meaning Washington State and Oregon, the volume of the 2011 timber harvest was 9 per cent above that of 2008. On the east side, meaning Montana, Idaho, and California, overall harvests are 5 per cent higher than in 2008. However, California is still 6 per cent below 2008 levels and Montana is 23 per cent lower.

"Log prices are 75 per cent higher than they were at the low point," detailed Lord.

For his part, Wikle explained that a lot of southern pine timber plantations have been converted to agriculture uses.

"There may be an impact on timber supply from that region going forward," explained Wikle.

On that topic, Marshall Thomas, President of F&W Forestry, provided some insight into southern US pine plantations.

"In the south, pine plantation owners are back to 1970s reforestation levels," said Thomas. "This is causing concern because they are not harvesting therefore not replanting. There are not a lot of young trees going into the ground in the south. Meanwhile, there is overcutting of natural pine forests, which is where most of the grade timber is coming from lately. It is possible that in ten to 15 years there will be issues with the supply of small wood, it is possible that by 2040 timber owners will have wiped out all the timber that is currently 20 years old.

"Or," continued Thomas. "There may end up being a bunch of really old trees which will never be harvested properly and another bunch of really young ones. The reality right now is that southern mills are dependent on supply from natural timber."

Keta Kosman
 Publisher
 Madison's Lumber Reporter
 Madison's Timber Preview
 Madison's Investment Rx
 www.madisonsreport.com
 604 984-6838