FEA Plantations Project 2008

Lonsec Agribusiness Research

April 2008

LONSEC

FEA Plantations Project 2008

LONSEC Recommended

Details	Option 1	Option 2	Option 3	Option 4
Location	Tasmania, NSW, Qld	Tasmania, NSW, Qld	Tasmania	Tasmania, NSW, Qld
Product	Eucalyptus sawlogs & pulp logs	Eucalyptus pruned sawlogs & pulp logs	Radiata sawlogs & pulp logs	4 Option 1 1 Option 2 2 Option 3
Target Woodlot size	7,500 ha 0.5 ha	1,000 ha 0.5 ha	500 ha 0.5ha	1,000 ha 3.5ha total
Target raising	$69 million			
Term	13 years	16 years	25 years	25 years
Level of Risk	Low/Mod	Low/Mod	Low/Mod	Low/Mod
Min outlay First year	$3,465*	$3,465*	$3,465*	$23,100**
Lonsec IRR (after-tax)	Mid-case **8.5 %**	Mid-case **9.1 %**	Mid-case **8.0 %**	Mid-case **8.8 %**
IRR Range	6.8% - 9.3%	7.6% -9.9%	7.2% - 8.4%	7.8% - 9.3%
Finance	Available from Forest Enterprises Australia Ltd (FEA)			
Commissions	Up to 10% (includes estimated marketing fees of 2%)			
ATO Ruling	PR2008/31	PR2008/32	PR2008/33	PR2008/34
Offer closes	30 June 2008			

*One Woodlot (including GST) **7 Woodlots (including GST)

Summary of Lonsec Rating

The FEA Plantations Project 2008 has achieved an overall rating for each option as follows:

Option 1: Recommended

Option 2: Recommended

Option 3: *Recommended*

Option 4: *Recommended*

The highest major determinant ratings were achieved for Forestry and Management, reflecting the strengths of FEA in these areas.

The lowest major determinant ratings were achieved for Industry, reflecting the challenges facing both the hardwood and softwood timber industries.

The Project Plan

- The Investment involves the growing of Shining Gum and Radiata Pine in Tasmania, and Sydney Blue Gum, Dunn's White Gum and Spotted Gum in NSW and Qld.
- Growers can select from 3 Options:
  - Option 1 for the production of sawlogs and pulpwood in NSW, Qld and Tasmania over 13 years.
  - Option 2 for the production of high value sawlogs and pulpwood and from pruned trees in NSW, Qld and Tasmania over 16 years.
  - Option 3 for the production of softwood high value sawlogs and pulpwood in Tasmania over 25 years.
- The upfront Establishment Fee of $3,465 per woodlot (inc. GST) applies to Options 1, 2 and 3. All other fees (except pruning fees for Options 2 and 4 in years 2, 4 and 6) are deferred until harvest at thinning and clearfall, and are paid as 15% (plus GST) of Harvest Proceeds for Options 1 and 2 and 10% (plus GST) for Option 3.
- Growers can also participate in Option 4, which is a combination of 4 Option 1 Woodlots, 1 Option 2 Woodlot and 2 Option 3 Woodlots, at a discounted Establishment Fee of $23,100 (inc. GST) for the 7 Woodlots (3.5ha).
- A Wood Purchase Agreement will be created between FEA Plantations Ltd (as the agent for Growers' wood) and FEA for all Options.
- Growers in Options 1, 2 and a portion of Option 4 have some protection of the returns via a floor price mechanism, set at approximately 85% of the expected Option 1 and 2 mid-case prices.

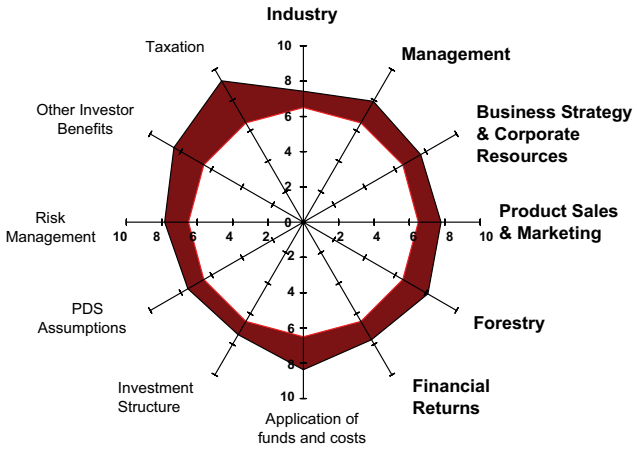
Key Project Drivers

- FEA Plantations Ltd (FEAP) is an established forestry investment manager, and since 1993 has established 15 MIS projects and has raised $279 million.
- FEAP proposes to delegate all woodlot management obligations to Forest Enterprises Australia Ltd (FEA), an experienced forest manager.
- Access to woodchip buyers with long term contracts via SmartFibre Pty Ltd, a joint venture with ITC Ltd.
- Value-adding via the downstream timber processing facilities owned and managed by FEA will provide potential for upside on Grower returns.

Key Project Risks

- Growth rates may be lower than expected
- Timber price may be lower than expected
- Market demand may be lower than expected
- Loss of key staff
- Changes in substance or interpretation of applicable laws relating to Income Tax, GST, environmental matters, native title

Lonsec Ratings: Weighted Average, all Options



The shaded area represents the amount by which the investment ratings exceed minimum approval score of 6.5.

Triggers for Review

- After the Research Report has been completed, Lonsec has asked to be notified of any significant changes, including supplementary offer documents, that materially or may materially affect the basis of our recommendation. This will allow Lonsec to reassess the recommendation.

Table of Contents

1. Lonsec Scope and Approach

Lonsec Agribusiness Research (Lonsec), a division of Lonsec Limited, has prepared this report for the Directors of FEA Plantations Ltd (FEAP).

1.1. Scope

The research process has included, but is not restricted to, the Lonsec Ratings Process using over 100 areas of assessment to rate the 12 critical determinants of an agribusiness investment. Lonsec has not engaged a solicitor to review the Project agreements, legal structure and FEAPs' due diligence process. Where applicable, Lonsec has commented on issues arising from a limited review of specific agreements, as noted in the report.

The ATO has issued Product Rulings PR 2008/31, PR 2008/32, PR 2008/33 and PR 2008/34 which apply to Options 1, 2, 3 and 4 respectively.

Lonsec has not engaged a taxation specialist to provide advice on the implications of the Product Rulings and proposed deductibility of the offer expenses to Growers.

Taxpayers who are considering participating in the Project are advised to confirm with their taxation advisers that changes in the law have not affected the Project's Product Rulings since they were issued.

The Product Rulings state that if the proposed arrangement is materially different from that which is actually carried out, the Rulings have no binding effect and will subsequently be withdrawn or modified.

1.2. Approach

Lonsec has rated the Project in accordance with the standard Lonsec rating methodology. Projects are assessed against a scale of 1-100, which is translated into the following descriptive ratings:

- Highly Recommended – 85 to 100,
- Recommended – 75 to 84,
- Investment Grade – 65 to 74,
- Not Approved – less than 65.

A Project must rate greater than 65 in each of the six Major Determinants - Industry, Management, Business Strategy and Corporate Resources, Product Sales and Marketing, Forestry and Financial Returns in order to pass as a whole, regardless of the total aggregate rating.

1.3. Sources of Information

This report has been prepared by Lonsec Agribusiness Research (Lonsec) for the Directors of FEAP. Lonsec has relied on information requested from FEAP, the PDS dated 19 March 2008 and information obtained from discussions with Project directors, management and key employees. Lonsec has also engaged Roger Underwood (Yorkgum Services, WA) as the Lonsec Consultant Forester to undertake a Forestry Review of the Project, and has relied upon the information supplied therein. The Lonsec Consultant Forester made visits to a number of the Project sites in November 2007 and January 2008. In addition, Lonsec has utilised information from the following sources in the course of preparing this report:

Product Disclosure Statement
FEA Plantations Project 2008 (ARSN 129 750 296) Product Disclosure Statement dated 19 March 2008

Expert Reports
VDFC Independent Forester's Report and Market Report
Lonsec Consultant Forester's Forestry Review Report

Material Agreements

Constitution	(FEAP)
Custodian Agreement	(FEAP and Tasmanian Perpetual Trustees)
Compliance Plan	(FEAP)
Management Agreement	(FEAP and Grower)
Head Management Agreement	(FEAP and FEA)
Deed of Guarantee	(FEAP and FEA)
Wood Purchase Agreement	(FEAP and FEA)
Forestry Right Deed	(Landowner, FEAP and FEA)
Forestry Right Lease Deed	(FEAP and Grower)

Licence, Product Rulings and Approvals
Australian Financial Services Licence No. 243515 held by FEAP.
ATO Product Rulings PR 2008/31, PR 2008/32, PR 2008/33 and PR 2008/34

Supporting Documents
FEA and FEAP biographies and qualifications of senior staff
FEA Annual Reports, 2003, 2004, 2005, 2006 & 2007
Manager's Reports to Growers, 2005, 2006 & 2007
FEA Environmental Management System Manual
FEA Draft Forest Safety Management System
AS/NZS ISO14001:2004 Environmental Management System Certificate of Approval
FEA Plantations Project 2008 Financial models (Grower and Manager)

2. SWOT Analysis

Strengths

- FEA is a well-established hardwood plantation manager with significant downstream processing facilities. FEA sells plantation timber in the form of woodchips, sawlogs, peeler logs or sawn boards.
- FEA has developed export wood fibre markets in Japan and China, as well as domestic sawn timber markets. As agents for the sale of Grower's timber, FEAP will enter into a Wood Purchase Agreement with FEA for the term of the project.
- Mid-range entry costs and deferred fee structures provide FEAP with an incentive to maximise project performance.
- The stumpage price assumptions for thinning and clearfall are conservative.
- A floor price mechanism provides a level of downside protection of Grower returns (Options 1, 2 and a portion of Option 4).

Weaknesses

- The Wood Purchase Agreement does not nominate specific volumes and prices. The timber will be sold as logs, effectively at the prevailing market price, having regard for the species, the location and the quality of the timber.
- Drought and flood losses are not covered by optional insurance. However, these risks are mitigated to the extent that the strict land selection procedures are implemented and by the provision of minimum stocking rate guarantees.
- The Independent Market Report concludes that the stumpage price assumptions are reasonable in the current market, however access to Australian price data for plantation hardwood sawlog products is limited.

Opportunities

- Strong worldwide demand for high quality plantation hardwood pulp including Chinese and South American pulp processors.
- High quality hardwood products attract premium pricing, with restrictions on access to native forest resulting in increasingly limited supply.
- As FEA grows its forest resource and processing facilities, it will become a stronger player vis-à-vis the Asian woodchip and timber buyers.
- FEA has completed a significant mill expansion to install large log sawing capacity, kilns, drying sheds and moulding/planing infrastructure. These facilities are expected to significantly increase the margins on the timber produced.

Threats

- Increasing production from maturing plantation resources worldwide could place downward pressure on international pricing within the Project term.
- With increasing national public awareness of environmental issues, the regulation and certification of environmental management has been subject to increasing public scrutiny and compliance costs.
- A general downturn in Asian economic conditions may result in reduced demand for timber based products.
- Improvements in paper recycling technology and increased recovery rates of recycled paper fibre may impact supply dynamics.

3. Key Drivers of the Project

Lonsec believes that the following key project components will drive the success of the FEA Plantations Project 2008.

3.1. Established Forestry Investment Manager

FEA has been involved in the development, promotion, management and financing of 15 MIS forestry projects since 1993. The total plantation area under management is approximately 50,000 hectares. Total subscriptions to the MIS projects are in excess of $280 million.

3.2. Expertise in Plantation Management

FEA's silvicultural and management expertise, together with the scale of its existing operations and its established and expanding presence in export timber markets, should allow the company to implement efficient practices relating to plantation establishment and management, harvesting, processing, and marketing, thereby bringing greater certainty to the achievement of the forecast Project yields.

3.3. SmartFibre Pty Ltd (formerly Tasmanian Fibre Pty Ltd)

In 2003 FEA, in joint venture with the Neville Smith Group (now part of ITC), formed Tasmanian Fibre Pty Ltd, and constructed a $9 million woodchip mill at Bell Bay in Tasmania. SmartFibre Pty Ltd (SmartFibre) has been regularly supplying wood fibre to Nippon Paper, Japan's largest pulp and paper manufacturer, since January 2007. SmartFibre has four contracts with Japanese customers to export both hardwood and softwood woodchip. In 2008, SmartFibre is expected to ship a total of 500,000 tonnes of export woodchips.

3.4. Value-adding Processes

Where possible, FEA will endeavour to market the harvested timber as unpruned sawlogs (which currently command a 20% to 25% premium to pulpwood price) or as pruned logs (up to 100% premium to pulpwood price). In addition, FEA currently operates a state-of-the-art integrated dry sawmill, which is specifically designed to process small diameter logs. This will allow the timber to be sold as sawn boards. FEA has recently completed a significant mill upgrade installing hardwood and softwood kilns, drying and moulding/planing capacity, which are expected to significantly increase the margins on the kiln-dried timber produced.

4. Investment Offer and Structure

4.1. Project Outline

The PDS for FEA Plantations Project 2008 (ARSN 129 750 269) is dated19 March 2008. The PDS constitutes a retail offer and the Australian Tax Office (ATO) has issued Product Rulings PR 2008/31, PR 2008/32, PR 2008/33 and PR 2008/34 in relation to this Project.

The Offer to Invest

FEA Plantations Limited (FEAP: ABN 44 055 969 429) is the Responsible Entity for the project, and FEA (ABN 47 009 553 548) is the parent company of FEAP, and financier of the Project.

FEAP has been granted AFS Licence number 243515, which gives FEAP the right to operate forestry managed investment schemes.

The offer is for Growers to establish woodlots in 0.5 hectare units, located in Tasmania, New South Wales and Queensland. The minimum investment in the project is one Woodlot with an area of 0.5 hectares.

Investment Options

Growers have the choice of four planting options:

- **Option 1:** Eucalyptus wood for sale as sawlogs or pulp logs over a 13 year term under which Growers pay a single Establishment Fee of $3,465 (inc GST) with no ongoing costs. Lease and management fees are deducted at 15% (plus GST) of Harvest Proceeds.
- **Option 2:** Eucalyptus wood for sale as high value sawlogs and veneer, as well as pulpwood, over a 16 year term under which Growers pay a single Establishment Fee of $3,465 (inc GST) and pruning fees of $396, $418, and $440 (inc GST) in years 2, 4 and 6 respectively. Lease and management fees are deducted at 15% (plus GST) of Harvest Proceeds.
- **Option 3:** Radiata pine wood for sale as high value sawlogs and pulpwood, over a 25 year term under which Growers pay a single establishment fee of $3,465 (inc. GST) with no ongoing costs. Lease and management fees are deducted at 10% (plus GST) of Harvest Proceeds.

- **Option 4**: Growers can also participate in Option 4, which is a combination of 4 x Option 1 Woodlots, 1 x Option 2 Woodlot and 2 x Option 3 Woodlots, at a discounted Establishment Fee of $23,100 (inc GST) for the 7 Woodlots (3.5ha). Lease and management fees are deducted from Harvest Proceeds. This option provides the greatest regional and product diversity, plus the benefit of a discount of approximately 5% on the Establishment Fee.

Timber Sales

Growers will receive a payment for wood sold following commercial thinnings, which are expected to occur in Year 9 for Options 1 and 2, Years 13 and 18 for Option 3, and Years 9, 13 and 18 for the relevant options within Option 4. Growers will also receive wood sale proceeds upon the final harvests.

FEAP will take on the responsibility as agent for the Growers to sell the harvested wood to FEA.

FEA is committed to entering into a wood purchase agreement for the purpose of purchasing wood grown under Options 1, 2, 3 and 4 (at thinning and final harvest) and is required to pay Growers a fair and reasonable price or the relevant Floor Price applicable to Options 1 and 2. Refer to Section 11.7 for more details.

Minimum Subscription

FEA Plantations has stated there is no minimum subscription for the Project to proceed, and has identified a target of 10,000 ha (20,000 Woodlots) for Woodlot sales in this project.

Establishment Fee

- Upon application, Growers in Options 1, 2 and 3 must pay an Establishment Fee of $3,465 (inc GST) per Woodlot, being the initial cost of preparing the land and the supply and planting of the seedlings. Growers in Option 4 must pay a discounted Establishment Fee of $23,100 (inc GST) for the 7 Woodlots (3.5ha).

Rent and Management Fee

- Rent and Management Fees are deferred until harvest. Growers in Options 1 and 2 will be charged 12% (plus GST) of Harvest Proceeds for Rent Fees, whilst Growers in Option 3 will be charged 7% (plus GST) of Harvest Proceeds for Rent Fees. Growers in Options 1, 2 and 3 will be charged 3% (plus GST) of Harvest Proceeds for Management Fees. These fees are deducted before distribution to the Grower.
- Option 4 Growers will be charged the fees as described above, in proportion to the components of Option 4, being 4 x Option 1 Woodlots, 1 x Option 2 Woodlot and 2 x Option 3 Woodlots
- Harvest Proceeds is defined as timber yield in cubic metres multiplied by the average stumpage price per cubic metre. Timber from the Project will be sold on a stumpage basis, with the buyer bearing the harvesting, transport, processing and marketing costs.
- This fee structure, by aligning the interests of the Responsible Entity with the interests of the Growers, provides the Responsible Entity with an incentive to maximise returns, for the benefit of both parties.

Pruning Fee

- Growers with Option 2 Woodlots will pay Pruning Fees of $396, $418 and $440 (inc. GST) per Woodlot in approximately years 2, 4 and 6. FEAP will index these fees in line with CPI.
- FEA Plantations will invoice Option 2 and 4 Growers by 30 June in the year that pruning has been completed.

Grower Finance

Applicants may apply to fund their investment through FEA up to a maximum of 100% of the Establishment Fee (inc GST), depending on the finance option selected.

4.2. Project Agreements

The relevant Agreements relating to the establishment of the Project are the:

- Constitution
- Management Agreement
- Forestry Right Lease Deed
- Wood Purchase Agreement
- Compliance Plan

The material agreements which govern or have an influence on the relationship between FEAP (as the Responsible Entity) and the Growers are summarised in section 16 of the PDS. Complete copies of these agreements are available on application from the Responsible Entity. Where applicable, Lonsec has reviewed the summary information provided in the PDS pertaining to the material agreements. Lonsec has not engaged a solicitor to review the Project agreements, legal structure and the Promoter Project due diligence process. As such, Lonsec has not provided a detailed assessment of these documents within the scope of this report.

Growers should also seek their own independent professional advice prior to entering into any of the Project Agreements.

Constitution

This document establishes the Project and is the primary document governing the relationship between FEAP and the Growers. It defines the Project terms, application process, management of project funds, business management, and legal rights and obligations that apply to the Responsible Entity and Grower under applicable laws and regulations.

Management Agreement

Under this agreement, the Grower appoints FEAP to be the Manager of the Project. The agreement includes relevant details pertaining to insurance, marketing, termination of the Manager, and force majeure conditions.

Under the Head Management Agreement FEAP delegates all woodlot management obligations to FEA including the Establishment, Maintenance, and Pruning Services, on agreed terms. All of these duties must be carried out in accordance with sound silvicultural practices.

Forestry Right Lease Deed

The Forestry Right Lease Deed is binding between FEAP, as Lessor, and the Grower, as Lessee. The deed outlines the rights for the Grower to effectively rent the land for the production of trees, under management by FEAP. The Grower will maintain all rights, title and interests in the trees and carbon credits unless the Lease Deed is terminated.

Wood Purchase Agreement

This agreement is to be established between FEAP and FEA for the sale and purchase of wood derived from Growers' Woodlots. The agreement specifies the determination of a fair and reasonable price, accounting for a range of relevant pricing, timing, and quality factors. This agreement also details the Average Comparative Price, which is determined by the average price paid over the prior two years for wood of the same or similar species, quality and quantity in the same region or state from which the timber was derived. The price offered for a specific log type, evaluated and approved by an independent expert, cannot be less than the Average Comparative Price or the relevant Floor Price. The Floor Price provision applies only to Options 1 and 2.

Compliance Plan

The Compliance Plan sets out the measures, processes, and procedures the Responsible Entity will use in managing the project to ensure compliance with the material project agreements, Corporations Act, ASIC policy, and the ATO Product Ruling specifications.

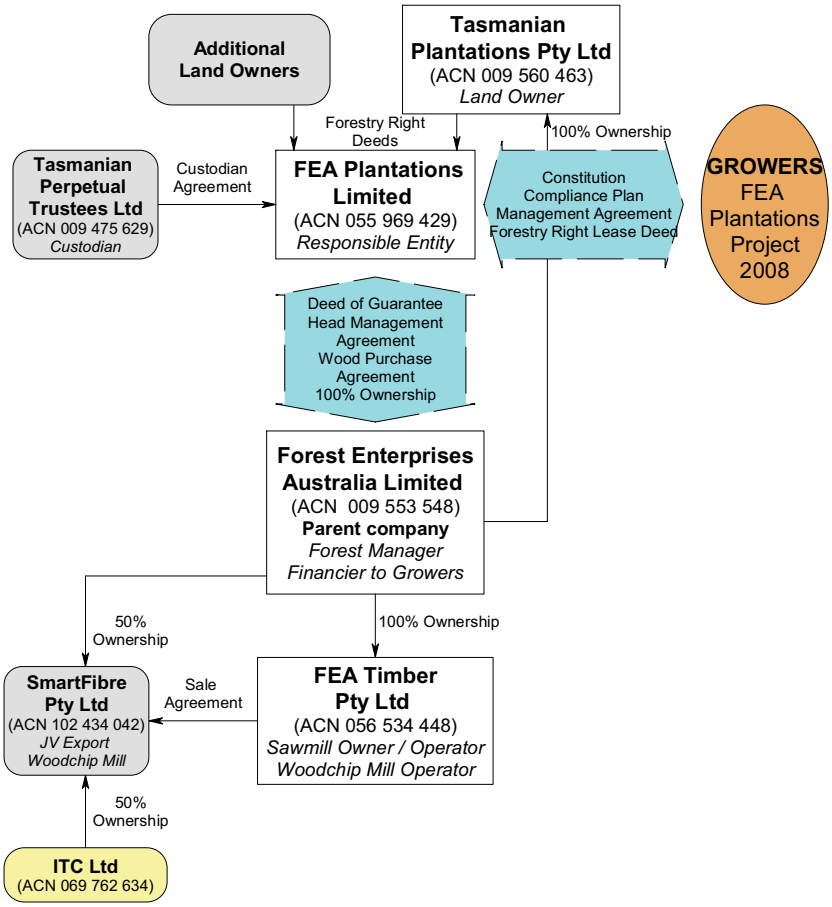
Project Documentation and Grower Information

FEA Plantations has information available to Growers via the FEA website or a toll free phone service. This information includes:

- Product Disclosure Statement – including supplementary amendments.
- Subscription Forms – including necessary application details.
- Independent Research – to review the investment proposal and provide comments on critical issues.
- ATO Product Rulings – these detail the deductibility of fees and payments.

4.3. Project Structure

Figure 4.1 Project Structure, including the external and Project related parties



5. Industry Outlook

5.1. Pulpwood

Pulpwood refers to wood sourced from both hardwood and softwood used in the production of pulp, which is further processed into paper and paperboard.

Japan is the main exporting market for Australian grown *Eucalyptus globulus* and *Eucalyptus nitens* pulpwood. The Japanese market has a preference for plantation grown pulpwood over native forest pulpwood due to its more consistent characteristics and higher pulpwood yields.

Certified forest products are increasingly attractive to Japanese buyers, particularly under the Forest Stewardship Council (FSC) system and the Australian Forestry Standard (AFS) system. Demand for certified products is likely to increase from all buyers in future and be a requirement to supply the world's largest users of pulpwood products.

Regions such as Indonesia, Thailand, Malaysia and China are currently cost competitive suppliers to the Japanese market but they are not expected to be major producers of export volume in the next five years, as it is possible that most will become net importers of hardwood pulpwood by 2012.

A significant hardwood plantation estate has been established in Australia under MIS structures since the mid-1990's. In FY2008 approximately 80,000 hectares will be established. This rate of establishment may not be sustainable because of the declining availability of suitable land and increases in land prices. The majority of the plantations established have been targeted at pulpwood for the production of hardwood woodchips for export.

The production from hardwood plantations will depend on future planting levels, with a reasonable estimate being 8 million m^3 pa from 2010. The volume of hardwood woodchips available from plantations is expected to increase in the next few years as the estate matures.

5.2. Sawn Softwood

The Australian softwood timber industry is a well established, commercial and viable industry with a solid history of production and economic performance. Australia's softwood plantation resource has attained sufficient size to support the industry and continue to supply markets and increase future export trade.

The key performance drivers of the industry have been identified by Lonsec as follows:

- Suitable land and climate for softwood plantation establishment and management
- Changes to Government policy which have promoted a shift away from native sawn hardwood production towards plantation softwood production
- Prolonged higher local consumption relative to local production, which under steady economic conditions is likely to exist into the future
- Local sawn softwood production continues to supply local markets and replace sawn softwood timbers that have historically been imported into Australia
- High export growth in new and existing markets, primarily of lower grade softwood timbers.
- Trends within the sawn softwood industry indicate growing demand for renewable construction products which in turn has provided the Australian softwood plantation industry significant growth opportunities.

5.3. Plantation grown Hardwood Sawlogs

Plantation grown hardwood sawlog volume is expected to grow rapidly, but from a very small base. Forecasts from the Bureau of Rural Services indicate that by 2040 plantation hardwood sawlog volume will be around 1.5 million m³ pa compared with the volume of plantation grown softwood sawlog which will be around 10 million m³ pa.

5.4. Hardwood Veneer

Veneer is produced from hardwood logs, which are ideally knot-free, and of high quality. Most of the hardwood veneer production in Australia is from native forest logs.

Common eucalypt species used for veneer production are Tasmanian Ash, Tasmanian Oak (60% of all sawn timber in Tasmania), Highland Oak and Stringybark Oak. *Eucalyptus globulus* (Blue gum) and *Eucalyptus nitens* (Shining gum) have also been found to be suited to veneer production. Other species used include Black Heart Sassafras, Golden Sassafras, Tasmanian Blackwood and Tasmanian Myrtle. Logs suitable for veneer are generally of higher quality than those used for woodchips.

Re-growth logs are generally smaller and prone to splitting at both ends; hence specialised equipment must be used to produce good quality veneer from these logs. Veneer cut from re-growth logs is said to be 'Crown Cut'.

Veneer is produced in thin sheets, obtained by either rotary peeling or slicing. Up to 1,000 slices can be obtained from one metre of log, making veneer production one of the most efficient uses of timber. The slices are joined into sheets called 'layons' which are then bonded to substrates, for example MDF or plywood. Veneer can also be used to produce laminated veneer lumber (LVL), whereby dried and graded wood veneers are layered with waterproof adhesive into blocks (billets), which are then cured in a heated press.

6. Management

The FEA group of companies includes Forest Enterprises Australia Limited (FEA) and its subsidiaries including FEA Plantations Ltd (FEAP), the Responsible Entity, FEA Timber Pty Ltd (FEAT), the sawmill operator, and Tasmanian Plantation Pty Ltd (TPPL), the land owning entity. In addition FEA hold a 50% interest in SmartFibre Pty Ltd, a woodchip export operation located at Bell Bay, Tasmania.

6.1. Forest Enterprises Australia Ltd (ABN 47 009 553 548) (FEA)

Established in 1985, FEA is a vertically integrated forestry and forest products company. FEA listed on the Australian Stock Exchange in June 2000 (ASX:FEA). The company's market capitalisation as at 14 April 2008 was $221 million.

6.2. Board of Directors of FEA

William Edwards
BA, LLB, MAICD
(Chairman / Non-Executive Director)

Edwards was appointed as a director of the Company in November 2002 and served as Chairman since November 2004. He is a legal practitioner with experience in property law, estate planning and company law and trusts.

Anthony Cannon
BSc (Forestry), MIFA, MACFA, MAICD
(Executive Director)

Cannon has been a director of the Company since 1985 and the Chairman of FEA Plantations Ltd since 1988. He has nearly 30 years of forestry experience and is responsible for project development, forestry industry and government relations, and forestry technical support. He received the World Forestry Day Award (Tasmania) in 1999.

Leslie Wozniczka
BSc (Hons), MBA (Non-Executive Director)

Wozniczka has served as a director of FEA since August 2005. He has substantial experience in financial advisory roles and capital markets. Currently, he serves on boards of Futuris Corporation Ltd, ITC and Australian Agricultural Company Ltd.

Michael Williams
BBus, CA, CFP, MAICD (Non-Executive Director)

Williams was appointed as a director of FEA in November 2002. He is an accountant by profession and is currently a principal of Camerons, a Tasmanian accountancy practice.

Desmond King
FAICD (Non-Executive Director)

King has been a director of the Company since December 2002. He has more than 50 years experience in the forestry industry in both the public and private sectors. He is a former CEO of Private Forests Tasmania and has owned and operated a forestry contracting business.

Donald C Taylor
B.Com, CA, Grad Cert. Rural Science, FAICD
Non-Executive Director, appointed 10/10/2007

Taylor is a Chartered Accountant with business, audit and taxation experience. He is the Chairman of Graincorp Limited (ASX listed) and also Chairman of the Graincorp Foundation. He is also a member of FEA's Audit and Risk Management Committee and the Remuneration and Nomination Committee.

Vincent Erasmus
Nat Diploma in Forestry (Sth. Africa)
Non-Executive Director, appointed 10/10/2007

Erasmus is the Chief Executive Officer of ITC Ltd. He has worked in the forestry industry for over 20 years, in both public and private sectors and in a range of roles encompassing logging, sawmilling, wholesale and industry development.

The Directors provide considerable experience in finance, agriculture, and business management.

The Board comprises four independent Directors and three non independent Directors.

The table below outlines the shareholding interests of the directors of FEA, as at 30 June 2007.

Table 6.1 FEA Shareholdings at 30 June 2007

Shareholder	No. of Shares	%
FEA Ltd Directors		
W D Edwards	12,276	0.003%
A M Cannon	7,206,861	1.779%
M J Williams	6,098,896	1.506%
D P King	16,250	0.004%
L P Wozniczka	0	0.000%
V M Erasmus	0	0.000%
Directors' Total	13,334,283	3.292%
Other Shareholders	391,665,717	96.708%
Total	405,000,000	100.0%

6.3. Senior Managers of FEA

Andrew White
B Sc (For), MAICD, MIFA
Chief Executive Officer

White has over 18 years experience in the forestry industry and has been CEO of FEA since 2003. White has previously worked for major Tasmanian forestry companies including Forest Resources (3 years), Boral Timber Tasmania (8 years), and Gunns (3 years) in range of senior management roles.

Fergus Leicester
B Bus (Acc), MBA, FCPA, FCIS, GAICD
Company Secretary & Chief Financial Officer

Leicester has over 15 years experience in the forestry industry and joined FEA in 2005, prior to which he held commercial/accountancy positions, including Boral Timber (8 years) and Gunns (5 years).

Anthony Cannon
Director, Forestry Services

Refer to comments in Section 6.2

Chris Barnes
General Manager, Plantation Operations

Refer to comments in Section 6.6

Andrew Wye
B Sc Forestry, Grad Dip Bus, MBA
General Manager, SmartFibre & Log Trading

Wye has had extensive experience in the forestry industry since 1987.

Ross Barlow
General Manager, FEA Timber

Refer to comments in Section 6.9

Doug Massey
BA, MBA
General Manager, Strategic Development – NSW/QLD

Massey is focused on special projects that will add value to FEA and its resources in the medium to long-term. He is based in northern NSW, a region which FEA has identified as the future growth area for the company.

Massey joined FEA and its Joint Venture, SmartFibre, in August of 2005 and was instrumental in the creation of the SmartFibre network. Prior to that he spent almost 13 years in Japan, with eight years at Daio Paper Corporation.

Michael O'Shea
MIFA
General Manager Business Development - Forestry

O'Shea is based in Lismore, northern NSW, and now oversees the Group's business development and carbon monitoring in Qld, NSW and Tasmania. With more than 30 years experience in the forest industry, O'Shea has held senior management roles including General Manager of ECI's Tasmanian consulting and contract forestry operations (Hazell Bros Group), Woodchip Mill Manager (Gunns) and Operations Manager (North Forest Products).

Kristen McPhail
BA (Economics), Dip Fin Planning, CIP
General Manager, Sales & Marketing

McPhail has had extensive experience in the financial planning industry since 1987. From 1999 she has specialised in the MIS forestry industry, working in management roles at the national level in the sales, marketing and business development areas.

6.4. FEA Plantations Ltd (ABN 44 055 969 429) (FEAP)

FEA Plantations Ltd (FEAP) acts as the Responsible Entity for MIS projects that are offered by FEA. FEAP has established 15 Eucalyptus MIS projects located in New South Wales, Queensland and Tasmania covering over 50,000 hectares. FEAP is 100% owned by FEA.

6.5. Board of Directors of FEA Plantations

Anthony Cannon (Chairman / Executive Director)

Refer to comments in Section 6.2.

Michael Williams (Non-Executive Director)

Refer to comments in Section 6.2

Gavin Wright
BA (Legal), CFP, Grad Dip Ed Admin, MAICD
(Non-Executive Director)

Wright is a director of the financial planning firm, Wright Planning Pty Ltd. He has experience in financial planning, compliance and forestry industries.

Kerry Duncan
LLB, MAICD (Non-Executive Director)

Duncan has over 30 years experience as a senior commercial/corporate lawyer with significant experience in the financial services industry. He was appointed Chairman of the Compliance Committee in 2005 and currently consults to the Victorian Department of Infrastructure.

The Directors provide considerable experience in finance, agriculture, and business management. None of the Directors or Senior Managers of FEA and FEA Plantations are listed on the ASIC Schedule of Disqualified Persons, Banned Securities Representatives, Banned Futures Representatives, or AFS Banned/Disqualified Persons.

6.6. Operational Management – Forestry Projects

FEA Plantations contracts all forestry operations to FEA. FEA has a 23 year history of forestry management in Tasmania and 7 years experience in NSW.

Chris Barnes
B Ag Sc (Hons), MBA
General Manager, Plantation Operations

Barnes joined FEA in 2007 after having worked in a number of forestry and horticultural managerial roles in Tasmania since 1994.

Andy Corbould
B Sc (Forestry)
Manager, Forestry Services

Corbould joined FEA in 2005 and oversees plantation management on behalf of MIS Growers and information systems, harvest wood-flow modelling, estate measurement, Grower reporting. Previous experience includes Forestry Tasmania, Forests NSW and Boral Timber.

Hugh Harris
B Natural Resources, M Resource Sc
Plantations Manager, NSW/Qld Plantations

Harris joined FEA in 2006, and has responsibility for coordinating the plantation establishment program in New South Wales and Queensland. Harris has 10 years experience in plantation forestry management and industry development.

Randal Jacobson
Diploma of Forestry
Manager, Land Acquisition, NSW/Qld

Jacobson has been with FEA since 1996 and is responsible for plantation establishment/ maintenance, harvesting operations, road operations, forest planning, management of forestry staff, land procurement and operational budgeting in NSW and Queensland. Prior to FEA, he operated truck and heavy machinery in forest operations and in agriculture.

Heath Blair
Certificate in Technical Forestry
Manager, Harvesting

Blair has had extensive experience in the Tasmanian forestry industry, in both the commercial and governmental sectors, since 1997.

Sven Rand
B Sc (Hons), MBA
Manager, Carbon Accounting

Since August 2007 Rand has been responsible for the strategic analysis of greenhouse gas sequestration and emissions throughout FEA's operations. He is assessing opportunities to provide value to the company and its Growers through participation in emerging carbon trading markets. Rand has been with FEA since 2000.

Lonsec believes the management of FEA and FEA Plantations are suitably experienced to manage the MIS woodlot projects.

6.7. Compliance Committee

FEA Plantations has prepared a compliance plan for the Project as required by the *Corporations Act 2001 (Cwlth)* to ensure that it meets its obligations as RE and that the rights of the Growers are protected. FEA Plantations has also established a Compliance Committee to monitor the extent to which FEA Plantations complies with the compliance plan. The compliance committee is comprised of two external directors and one internal director.

The members of the Compliance Committee are:

- Ross Waining B Sc (Forestry), External Member
- Nigel Dawkins B Bus (Acc), CA, External Member
- Kerry Duncan LLB, MAICD, Internal Member

6.8. Tasmanian Plantation Pty Ltd (ACN 009 560 463) (TPPL)

TPPL is the FEA's land owning entity, holding all of that part of FEA's forest estate which is owned rather than leased. TPPL is 100% owned by FEA.

6.9. FEA Timber Pty Ltd (ABN 67 056 534 448) (FEAT)

FEA Timber operates FEA's sawmilling and timber processing operation, located at Bell Bay, Northern Tasmania. The mill is utilises a specialised North American designed sawmilling process called an Optimil. FEA Timber is 100% owned by FEA.

Ross Barlow
MBA
General Manager FEA Timber

Barlow joined FEA in 2007, prior to which he held management positions at CHH Panels Bell Bay (4 years), and Rayonier MDF New Zealand (2 years).

Trevor Innes
BE (Hons), PhD
Manager, Timber Technology

Innes has been Manager, Timber Technology for FEAT since 2006. He has previously worked at the University of Tasmania as tutor, lecturer and post-doctoral research fellow. He also worked as the Technical Manager of the Timber Research Unit, School of Architecture and as technical advisor to industry.

Dale Jessup
Manager, Operations

Jessop has been Manager, Operations for FEAT since 2005. Prior to that he had extensive experience with Frenchpine from 1984.

6.10. SmartFibre Pty Ltd (ABN 33 102 434 042) (SmartFibre)

SmartFibre is a 50/50 joint venture formed in March 2003 between FEA and ITC. Ltd (ITC) which owns and operates a $9 million woodchip export facility located at Bell Bay, Northern Tasmania. SmartFibre sources sawn timber residues and pulplogs from FEA Timber and other suppliers then markets the pulpwood fibre as SMARTFIBRE™ to Chinese and Japanese customers.

7. Business Strategy and Corporate Resources

7.1. Company Background

Forest Enterprises Australia Limited (FEA) is a publicly listed company (ASX: FEA) which specialises in forest plantation management, plantation sawn timber products and wood fibre processing and exporting. At present the company has in excess of 50,000 ha of hardwood and softwood plantations under management, which are managed to produce woodchips, sawn timber, poles and peeler logs on behalf of managed investment scheme (MIS) investors and on its own account.

Company Structure – The FEA Group is vertically integrated into the timber supply chain with involvement in the sale of MIS products, development of plantation resources and processing and sale of timber products.

Business Strategy – FEA continues to build a land bank through freehold and lease acquisitions. This, in conjunction with strategic involvement in timber industry R&D and vertical integration, has put FEA in a strong position for future growth.

Management – The corporate management team at FEA has the appropriate experience to successfully manage its activities. The operational activities are predominately carried out by FEA staff, with harvesting and transport contracted to external parties.

Production capacity – FEAT operates FEA's sawmilling and timber processing operation located at Bell Bay in northern Tasmania. This state-of-the-art mill utilises a new specialised Canadian designed sawmilling process known as an Optimil.

The $72million sawmill, utilising North American technology, has been constructed on the former Carter Holt Harvey site at Bell Bay. It was commissioned in March 2008 and is capable of processing large logs up to approximately 80cm in diameter. The key aspects of the mill expansion are:

- The mill will process 450,000 tonnes in the first full year of operation
- With this additional capacity FEAT will become Tasmania's largest plantation sawmiller
- The mill is unique in Australia for the diversity of sawn timber products it produces: hardwood and softwood, structural and decorative
- FEA has entered into a 10 year contract with Timberlands Pacific Pty Ltd (formerly Rayonier Australia Pty Ltd) for the supply of 290,000 m³ of softwood per annum to ensure continuity of wood supply to the processing operations.
- In addition, three high temperature, high speed, drying kilns for softwood will be installed, together with a low temperature kiln for hardwood

SmartFibre is a 50/50 joint venture formed in March 2003 between FEA and ITC Limited, which owns and operates a $9m woodchip export facility located at Bell Bay, northern Tasmania. SmartFibre sources sawn timber residues and pulplogs from FEAT and other suppliers and then markets the pulpwood fibre as SmartFibre to Japanese customers. SmartFibre also secured 5 year woodchip forward supply contracts in both hardwood and softwood with major Japanese pulp and paper companies during 2007.

7.2. FEA Limited strategic objectives

The company's business strategy is focussed on the following key strategic objectives. FEA believes that the development of this strategic approach will deliver superior returns to Shareholders and Growers.

Vertical integration of the forestry and forest products operations

FEA has expanded its Forest Products segment to support the strategic direction towards vertical integration. The integration process has delivered business opportunities and has identified further opportunities that will be targeted in the future.

Development of a high quality, substantial, independent private forestry resource

FEA controls a substantial private forest resource. This includes not only hardwood plantations managed for about 9,000 growers, covering in excess of 50,000 hectares (after completion of current establishment obligations), but also 290,000 tonnes a year of softwood sawlogs purchased under a long-term contract. These two resources enable FEA to reach commercial economies of scale and market a range of competitive products.

Expansion of processing and marketing capacity

FEA has increased company resources and capacity to manage the expanded operations. Staff resources have been increased to support the construction of the new sawmill at Bell Bay and develop markets prior to the start of full production in April 2008.

7.3. Financial Resources

The table below illustrates the growth of FEA's balance sheet over a three year period.

Table 7.1 Summary of FEA Consolidated Financial Statements – 2005 to 2007

Forest Enterprises Australia Ltd	AIFRS	AIFRS	AIFRS
Year ended 30 June	2005	2006	2007
SEGMENT REVENUE ($m)			
Forest Products	22.8	16.9	20.6
Managed Investment Schemes	44.9	67.5	79.7
Unallocated revenue	0.8	0.7	1.4
Reported Revenue	68.5	85.1	101.7
PROFIT AND LOSS ANALYSIS ($m)			
Lonsec Adjusted Operating Revenue *	63.6	77.7	94.4
Other Revenue	4.9	3.5	4.3
SGARA	0.0	4.0	3.0
Reported Revenue	68.5	85.1	101.7
Lonsec Adjusted Revenue	**68.5**	**81.1**	**98.7**
Earnings Before Interest and Tax (EBIT)	20.8	27.9	28.3
Interest Income	1.9	3.2	3.8
Borrowing Cost	(0.5)	(1.1)	(2.1)
Reported Profit Before Tax	22.2	30.0	30.1
Lonsec Adjusted Taxation Expense	(6.6)	(7.9)	(7.7)
Lonsec Adjusted Net Profit After Tax (before asset revaluations)	**15.6**	**18.2**	**19.3**
EBIT/Sales Margin	**30%**	**33%**	**28%**
Adjusted Return on Equity	**14%**	**11%**	**8%**
Interest Cover (Times)	**n/a**	**n/a**	**n/a**
SUMMARY BALANCE SHEET ($m)			
Current Assets	80.2	83.5	133.2
Non-Current Assets	145.8	214.5	309.5
Total Assets	**226.0**	**298.0**	**442.8**
Current Liabilities	77.9	80.6	112.8
Non-Current Liabilities	14.2	31.0	41.8
Total Liabilities	**92.1**	**111.6**	**154.6**
Net Assets	**133.9**	**186.3**	**288.1**
Working Capital Ratio	**1.03**	**1.04**	**1.18**
GEARING ($m)			
Long Term Debt	1.0	11.5	11.8
Short Term Debt	1.0	1.3	30.4
Less Cash at Bank	17.9	13.2	42.5
Net Debt	**(15.9)**	**(0.3)**	**(0.3)**
Net Debt/Equity	**0%**	**0%**	**0%**
SUMMARY CASH FLOW ($m)			
Opening Cash	9.8	17.9	13.1
Operating Cash Flow	20.3	18.8	6.1
Investment Cash Flow	(39.0)	(55.5)	(97.5)
Financing Cash Flow	26.8	31.9	120.8
Net Cash Flow	8.1	(4.8)	29.5
Closing Cash	**17.9**	**13.1**	**42.5**

* Reported operating revenue less SGARA and interest income

Revenue

In FY2007, FEA generated Lonsec adjusted operating revenue of $94.4m, an increase of 22% from $77.7m in FY2006. This produced a FY2007 NPAT of $19.3m, up by 6% on the corresponding FY2006 figure of $18.2m.

Reported total revenue of $101.7 for FY2007 has two major components; MIS revenue $79.7m (78%) and forest products revenue $20.6m (20%). This represents an increase in reported revenue of 19.6% compared to FY2006. By comparison, revenue growth from FY2005 to FY2006 was 24.1%.

Despite the challenging market for MIS products during FY2007, FEA has maintained sales equivalent with the previous year and managed to increase market share.

MIS sales

MIS sales in FY2007 remained steady at $60.2m compared with $61.0m in the previous year. Total revenue during 2007 increased by 19.6% on the previous year, aided by the strong growth in forest products and recognition of the previous year's MIS income.

FEA's market share of MIS sales has demonstrated consistent growth over the last 5 years and is likely to underpin the company's continuity of log supply into the future.

Balance sheet

As at 30 June 2007, FEA had net assets of $288.1m, up from $186.3m in the prior year. FEA has a strong cash and debt position with bank finance facilities recently increased to $130 million.

As at 30 June 2007 the FEA Group did not have any net debt (cash and cash equivalents exceeded borrowings). The lack of gearing contributes to FEA's low Return on Equity, as shown in Table 7.1 above.

Cashflow

Net cash flows increased to $29.5m in FY2007 after recording an outflow of $4.8m in the previous year.

Director's Shareholdings

Table 6.1above outlines the shareholding interests of the directors of FEA Ltd, as at 30 June 2007. In addition, the Directors own 369 Woodlots in various MIS projects as at 30 June 2007.

7.4. Managed Investment Scheme Summary

FEA Plantations has offered 15 projects since 1993, raising a total of $279.1m.

Table 7.2 Previous Projects offered by FEA Plantations

Project Name	Year	Hectares Planted	Total Investment ($m)
Tasmanian Forests Trust No. 1	1993	52	0.1
Tasmanian Forests Trust No. 2	1994	165	0.5
Tasmanian Forests Trust No. 3	1995	186	0.7
Tasmanian Forests Trust No. 4	1996	222	0.8
Tasmanian Forests Trust No. 5	1997	376	1.3
Tasmanian Forests Trust No. 6	1998	928	4.1
Tasmanian Forests Trust No. 7	1999	10,826	50.8
Tasmanian Forests Project 2000	2000	2,006	9.2
Australian Forests Project 2001	2001	1,293	7.0
Australian Forests Project 2002	2002	409	1.8
Forest Enterprises Plantation Project 2003	2003	2,210	11.1
FEA Plantations Project 2004	2004	4,369	26.3
FEA Plantations Project 2005	2005	9,026	54.1
FEA Plantations Project 2006	2006	10,686	67.3
FEA Plantations Project 2007 (Released 5 May 2007)	2007	6,994	44.0
Total (as at 30 June 2007)		**49,748**	**279.1**

FEAP has offered 15 projects since 1993, raising a total of $279.1m to 30 June 2007. In FY2006, FEAP launched its first project with a longer-rotation pruned sawlog option targeting veneer, and decorative select grade timber product markets.

Lonsec has examined the reports prepared in March 2007 by FEAP and the Independent Forester, Gerry Cross of Van Diemen Forestry Services Pty Ltd, to the Growers in all of these projects, except the FEA Plantations Project 2007.

The Independent Forester reports that, in general, the state of progress of all projects is on schedule, with most plantations exceeding expectations and a few marginally lagging expectations. In the latter case the manager has been actively managing the situation by:

- Controlling weeds until the canopy closes and shades the inter-row area, thereby discouraging weed growth.
- Active control of insect pests. In NSW and Queensland there are two species of psyllid one on the *E. dunnii* and one on *E. grandis* which are now showing up as an insect pest to be monitored and managed in these regions. FEA has appointed a graduate forester to look after stand protection as a sole responsibility. This person has devised and put in place a process to monitor the plantations on a routine basis and if necessary organize activities such as spraying for these insect and fungal pests as well as fertiliser applications for any observed nutrient deficiencies.

- Monitoring of nutrient levels and, where necessary, the application of fertilisers or trace elements.

FEA has experienced only minor losses due to fire during its 22 year history, with 150ha of a Walcha, NSW plantation experiencing fire damage in August 2006. All growers affected received full investment insurance compensation.

Cattle are being agisted on selected plantations to limit the growth of weeds between rows and on the firebreaks. Firebreaks and fire tracks are well maintained and the manager maintains an active fire plan with duty and stand-by rosters.

FEAP will complete its first managed forestry project (15 year term) in May 2008 which is forecast to deliver a 7.5% after tax return to Growers. The Project (1993) is expected to produce a total yield of 417 tonnes (MAI of 29.2) and total harvest proceeds distribution of $17,400 (incl. GST).

For the six projects established in the period 1993 to 1998 inclusive, FEAP has taken inventory measurements which indicate that the average MAI (Total Stem Volume) at age 15 could range from 21.9m^3/ha/year to 34.7m^3/ha/year, with a weighted average of 25.5 m^3/ha/year.

Growers in FEAP's first two projects (1993 and 1994) have received final returns from thinnings (totalling $2,622/ha and $2,540/ha respectively). Thinning yields were in line with expectations (90-100t/ha) and prices were confirmed by the Independent Forester as being high relative to market value.

Thinning operations and payments for the 1995 Project ware completed by the end of 2007 but only 60% of the project was available for thinning because of the steep terrain. Growers received a thinning return of $1,354/ha. Thinning operations and payments for the 1996 Project are scheduled to be completed by the end of FY2008. Only 60% of the project is expected to be available for thinning because of the steep terrain.

7.5. Research and Development

FEA has a research and development facility which is run by Dr Trevor Inness. This includes R&D plant and equipment formerly used by the University of Tasmania. FEA also contributes to research programs and has formal and co-operative links to following organisations:

- Co-operative Research Centre for Forestry, based at CSIRO and the University of Tasmania in Hobart. Various working groups on nutrition, protection from insects, disease and vermin, and tree breeding.
- Southern Tree Breeding Association *E. globulus* tree breeding program.
- Queensland Department of Primary Industries and Fisheries. Taxa trials, tree breeding, nutrition and species/site matching.
- Browsing Damage Management Group. Mammal browsing (linked to Tasmanian Institute of Agricultural Research).
- Southern Cross University in Lismore. Forestry undergraduate and PhD students are employed in some plantation work and local staff act as field guides and tutors for some of their subjects.
- Supporting partner of the CRC Forestry in Hobart.
- Member of Subtropical Forest Health Alliance.

8. Product Sales and Marketing

8.1. Buyers and Marketing

FEA and SmartFibre Pty Ltd have established relationships with major Japanese trading houses and leading pulp and paper manufacturers throughout Asia.

SmartFibre currently exports approximately 500,000 tonnes of woodchips per annum to Japan. Contract terms and price setting arrangements vary between customers and years. Each year woodchip prices are based on the Australian benchmark hardwood chip price (LAHCE). The 2008 headline plantation hardwood woodchip price from Bell Bay is AUD198.50/BDMT.

8.2. Wood Purchase Agreement

The Management Agreement appoints FEAP to market the pulpwood and sawlogs on behalf of the Growers. FEAP then intends to enter into a Wood Purchase Agreement with FEA for the sale of pulpwood and sawlogs supplied from Growers' woodlots. FEA must accept all the saleable wood harvested and delivered in accordance with the harvest plan. However, should an agreement not be reached for any reason, FEAP may accept offers from interested third parties, with FEA holding the first right of refusal.

Determination of Purchase Price

A number of key factors are set out in the Wood Purchase Agreement (WPA) which FEA must account for in the determination of a "fair and reasonable" purchase price. These key factors include:

- The proposed end-use of the wood;
- The price or prices being paid by other bona fide wood processors for wood of the same or similar species, quantity and quality in the state or region where the plantation is located and the price or prices in other states or regions of Australia;
- Customary methods of determining the price of wood of the same or similar species, quantity and quality in other states of Australia;

- The quality of the wood to the extent that it would affect the purpose to which the wood will be put;
- The timing of the commencement of harvesting so that the wood being sold to FEA is harvested and marketed in an orderly way; and
- Relevant information supplied by any party including statistics or indices relevant to wood prices published from time to time by the Australian Bureau of Agricultural and Resource Economics, the Australian Bureau of Statistics or any other government authority or industry body.

The WPA specifies that the purchase price paid to growers will not be less than the Average Comparative Price. The Average Comparative Price is the average price paid by FEA or other major plantation timber purchasers to other major plantation timber suppliers over the two preceding years for wood of the same or similar species, quality and quantity as the wood in the region or state in which the plantation is located. In determining the Average Comparative Price, FEA Plantations will exclude prices paid for wood where the volume levels are not material or where the terms of the sale were not at arms length.

The RE must not sell the timber for the purchase price until it has had the purchase price independently evaluated and approved by an independent expert.

Lonsec notes that publicly available comparative pricing benchmarks are difficult to establish, particularly for entities that are not participants in the export trade, and where benchmarks are quality and quantity specific. The issue is further complicated by the related party transaction process, with FEA Plantations (a wholly owned subsidiary of FEA) allocated as agent for the Growers' timber products.

FEA Plantations may seek offers from interested third parties. Alternative offers must be presented to FEA which then has one month to agree to the higher price or to refuse the offer. To this extent, Growers will largely be reliant on the transparency of pricing negotiations between FEA Plantations and FEA, and independent advice that the price being offered is fair and reasonable.

Determination of Grade and Quantity

Growers' wood will be graded in accordance with the Harvest Plan and recognised industry standards, as agreed to by FEA Plantations. The WPA states that the quantity of wood purchased must be determined by weight and measured by a weighbridge nominated by FEA. Where it cannot be determined by weight, the quantity will be determined by any other reasonable method used within the forestry industry and agreed to by FEA Plantations.

Floor price mechanism

A detailed description as to how the floor prices are determined for Options 1 and 2 is given in Section 11.7 – Summary of Assumptions

Ownership and Risk

The WPA states that ownership and risk in relation to the wood passes to FEA only when the wood is delivered to the location nominated by FEA in the Harvest Plan and the wood is accepted by FEA as meeting the specifications of the Harvest Plan.

Pooled Harvest and Distribution of Proceeds

The Gross Proceeds from harvesting are determined by the prevailing quality, quantity and price of the Growers' timber at harvest, under each option. The Gross Proceeds will be pooled collectively for all Growers who have contributed to returns in that option.

With woodlots established over multiple properties located across Tasmania, NSW and Queensland, Individual Growers will be protected from events which reduce the yield or quality from their individual Woodlot(s). Once pooled, gross harvest proceeds are then subject to applicable fees including the deferred lease and management fees (plus applicable GST).

9. Forestry Review

9.1. Lonsec Consultant Forester's Report

Lonsec has commissioned a Lonsec Consultant Forester's Report which provides a review of the forestry aspects of the FEA Plantations Project 2008. A summary of the Lonsec Consultant Forester's Report is provided below and comments regarding principal forestry risks and commercial investment risks are included in section 12 of this report.

Extracts from the report prepared by Lonsec's Consultant Forester are reproduced below. Lonsec recommends that prospective Growers read these extracts from the report before making a decision to invest in FEA Plantations Project 2008. Lonsec also refers Growers to the Independent Forester's Report and the Independent Market Report provided in section 13 of the PDS for additional and detailed Project information.

Specific quotations from the Lonsec Consultant Forester's Report are identified in italics.

9.2. Review of Documentation

The Consultant Forester has:

- *Read the PDS for the project prepared by FEAP and a range of other documents provided by FEA and others during this review.*
- *Inspected the seed certificates from CSIRO and Seed Energy. They provide clear information about the eucalypt seed to be used by FEA.*
- *Inspected FEA's Environmental Management System and their operational manual and found them to be comprehensive, professionally prepared, and clear about who is responsible for outcomes.*
- *Been briefed by FEA on their accreditation to ISO 14001:2004 and SmartFibre's Chain of Custody arrangements to satisfy the Forest Stewardship Council's Controlled Wood Standards, and on the procedures associated with annual audit and reporting of operations to ensure on-going accreditation. FEA advises that it is aware of the requirements placed on the company by State Forestry Codes of Practice in Tasmania, NSW and Queensland, and that FEA will comply with all three. FEA has achieved accreditation by the Australian Forestry Standard for plantation operations in Tasmania, and advises that they hope to achieve this for NSW/Qld operations during the first half of 2008.*

9.3. The Project

Three hardwood tree species are to be planted in three regions.

- *E nitens (shining gum or "nitens") will be planted in Tasmania and the southern tablelands region (south of Armidale) of NSW;*
- *E dunnii (Dunn's white gum or "dunnii") and Corymbia citriodora variety variegata ("CCV" or "spotted gum") will be planted in northern coastal NSW and southern Queensland. Dunnii will be planted on lower lying areas subject to frost, and spotted gum on the upper slopes and ridges.*

The PDS mentions other species, including flooded gum (E grandis) and blackbutt (E pilularis) which may be planted as part of this project, but FEA stated that this is unlikely. Flooded gum is subject to a serious pest problem, while the site requirements for blackbutt are too particular. Neither of these two species is further considered in this report. FEA advised that they will extend trial plantings of E saligna (Sydney blue gum) on frost-susceptible sites to further test its suitability as a back-up species for dunnii, and of the highly promising new spotted gum hybrids which are being developed by researchers in Queensland. The consultant is pleased to see these trees included in the Project as trials, as both are fine tree species suited to the locality, and with good commercial value.

It is envisaged by FEA that approximately 80% (8,000 hectares) of the 2008 project will be established in NSW/Queensland, and 20% (2,000 ha) in Tasmania. Virtually all of the Woodlot Option 2 plantings will be in Tasmania.

9.4. The Industry

The Plantation Industry in Tasmania

The forest industry including plantation forestry (predominantly comprising short-rotation pulpwood production from eucalypts, but these days increasingly incorporating longer rotation plantations which will produce higher value products) is a vital element in Tasmania's economy and labour market. The plantation sector continues to expand, and enjoys strong government support.

The technology for commercial plantation growing with E nitens and P radiata is well-understood. There are protocols for site selection, nursery practice, site preparation, establishment, weed and pest control, bushfire control, silviculture and harvesting. There has been a program of silvicultural research stretching back for decades. Plantation growers have access to high quality genetically improved seed. FEA has been harvesting mature eucalypt plantations since 1997 and has been milling plantation-grown sawlogs (pine and eucalypt) and exporting woodchips for four years. FEA has tested the overseas market for export of plantation grown logs, and has sold (either directly or through agents) several whole or part shipments of high value peeler logs to China, Japan and Malaysia. This is a market opportunity which may increase.

The biggest problem for the expansion of plantation forestry in Tasmania is availability of suitable land. The most desirable land is freehold cleared land in areas receiving >950 mm annual rainfall, for which there are many competing interests. FEA expects to continue to acquire new land in Tasmania, either through purchase or leasing, but increasingly their eucalypt plantations will be grown as second or third rotations on the same sites.

Two issues affecting forestry in Tasmania are opposition from sectors of the community to plantation development on farmland and concerns about the need to control native browsing animals at the time of plantation establishment. These concerns make it difficult to acquire land in some areas e.g., southern Tasmania, or result in increased costs for establishment and management.

FEA is a leader in the Tasmanian forest industry in four areas.

1. *FEA has developed a fully vertically integrated system which maximises sawlog recovery, and minimises waste. The centre-piece of this system has been the unique sawmill at Bell Bay incorporating a Finnish HewSaw, which has now been updated to a $72 million state-of-the-art Canadian Optimil facility.*

This is capable of producing high value sawn timber (marketed as EcoAsh®) from both large and small logs. High quality sawing is supported by sophisticated drying technology, using imported kilns. EcoAsh® is able to compete successfully with radiata pine in the marketplace and can be used for a variety of purposes. Point 4 below details the new sawmill facility.

2. *FEA has been able to secure endorsement from the Forest Stewardship Council's certifiers, that woodchip production for their SmartFibre product meets FSC's Controlled Wood Standards. This ensures acceptability to overseas buyers.*
3. *FEA has developed their own wood technology laboratory, on site at the Bell Bay mill. This allows research and development into wood products, and on-site engineering testing of timber products.*
4. *FEA has commissioned a new ultra-modern sawmill and processing plant at Bell Bay. This incorporates an imported Canadian Optimil, which is state-of-the-art sawmilling technology and will be superior to the HewSaw in dealing with larger plantation grown sawlogs, and will significantly increase the recovery of sawn timber.*

Final decisions are pending on the construction of a pulpmill by Gunns Ltd at Bell Bay in Tasmania. This will purchase both eucalypt and pine woodchips from plantation thinning or as a by-product of sawlog production. Approval from the Tasmanian government and conditional approval from the Federal government have been achieved. If the pulpmill goes ahead, as seems likely, it will significantly benefit FEA, either directly by providing a domestic buyer for their woodchips and sawmill waste, or by freeing up a large volume of potential woodchip market in Asia which will no longer be supplied by Gunns.

The NSW and Queensland Region

FEA has been establishing eucalypt plantations in the central highlands region and the northern coastal region of NSW, and in south eastern Queensland since 2001. Initially the intention was to produce mainly pulpwood, but the emphasis has shifted to growing sawlogs and utilizing thinnings or mill waste for pulpwood production.

The principal area targeted by FEA is roughly 200km in radius from Brisbane Port. This encompasses areas around Kingaroy in Queensland down to Grafton in NSW. All of this area has a subtropical climate with an all-year round (but summer maximum) rainfall generally greater than 1,000 mm/yr. The winters are generally cool, with occasional mild frosts in the lowlands. The area suffered a serious drought during 2002/3, an event which may re-occur, and rainfall in south-east Qld has been mainly well below average for several years, but currently both regions are enjoying excellent growing conditions.

The NSW central highlands region south of Armidale has a warm moist summer and a cold winter and is suitable for growing shining gum.

The Consultant Forester has not inspected the FEA plantations in this area, but is familiar with the region and its potential, and has reviewed the results of research plantings by State Forest NSW.

Shining gum is indigenous to this region and it should be possible to produce eucalypt sawlog and pulpwood from professionally established and managed plantation. FEA advises that their early plantations have suffered from fungal pest infestation which has been difficult to control, but with improved nutrition they are hopeful this can be overcome. In addition, from 2008 FEA will be using the Northern Provenance of shining gum in this region and this will be better adapted to local conditions and better able to handle fungal infection.

Forestry in northern NSW and southern Queensland has special characteristics and requirements:

- *There is limited history of eucalypt plantations in the region, on which to base operational techniques and yield and cost and price projections. FEA is a pioneer in this region.*
- *Although rainfall averages are high, droughts can occur, leading to establishment difficulties in some years. In dry years, especially in Qld, it will be necessary to water-in newly planted seedlings, or to replant failed areas the following year (which FEA guarantees to do if required).*
- *Frosts are common in low-lying areas and species such as spotted gum will be killed if planted too low in the landscape. Designation of species to sites must be done at the micro-level by experienced foresters.*
- *Weed growth in warm moist conditions (which occur for most of the summer months in Queensland and northern NSW) is rampant, and the most rampant weed growth occurs at a time when the plantations are so wet that control measures cannot be taken. Under these conditions, weeds cannot be eliminated, but must be managed to minimise their impact on tree survival and growth. It is noted that FEA are using helicopters to spray weeds where conditions are too wet for ground-based application, and that this is effective, especially in minimising weed competition with recently planted seedlings.*
- *Leaf-eating insects and fungal pathogens are favoured by warm moist conditions, and can become a problem very rapidly if not detected and controlled. Effective pest management is absolutely critical for plantation success in this region, especially with E dunnii which is readily attacked by a number of pests.*
- *Genetic improvement of the species to be planted by FEA is not well advanced.*

- *Brisbane Port is nearly three days less sailing time to woodchip buyers in Asia than is northern Tasmania, and the moisture content of the timber is lower than that grown in Tasmania, making the woodchips more valuable. Alternatively, residue material (including woodchips) may be processed locally and sold into the Australian domestic market.*

Assessment of species being planted

The following table summarises the strengths and weaknesses of the five species to be planted by FEA in this project:

Species	Common name	Strengths	weaknesses	Comments
E. nitens	*Shining gum*	*Valuable tree with high commercial value, genetically improved material available; long experience with plantation silviculture and timber utilisation in Tasmania;*	*No major weakness when planted in Tas. Planting in NSW must employ a suitable provenance, or will suffer from fungal attack on juvenile foliage.*	*A proven species, with versatile timber, suitable for both pulp and paper manufacture and high quality sawn timber*
P radiata	*Monterey pine*	*The most widely used timber tree in plantations in Australia. Very well established silviculture; genetically improved seed is available*	*No major weakness. High quality genetically-improved seed available. Effective fire protection essential*	*Excellent softwood species with wide commercial acceptance and applications*
E dunnii	*Dunn's white gum*	*Prospectively a desirable hardwood plantation species, with high early growth rate; frost tolerant. Wood has good fibre qualities for pulp and paper manufacture.*	*Susceptible to a range of insect pests (esp Pysillids); more research required into genetics, nutrition and, growth patterns. Sawing technology is still in the trial stage*	*Early plantation performance is promising where defoliating insects controlled. There are no mature plantations on which to judge actual outcomes/returns.*
*CCV**	*Spotted gum*	*A tough tree with excellent timber, and a high degree of acceptability in the sawmilling and timber-using industries.*	*Susceptible to a fungal pest which can deform the stem and reduce growth rates; knowledge about genetics, nutrition and growth patterns still evolving. Good quality pulp, but not widely used at this stage for pulp and paper manufacture.*	*Should perform well, if the right provenance is used and stands are properly managed to reduce the risks of fungal attack.*
E saligna	*Sydney blue gum*	*A fast growing tree with excellent timber, including red heartwood. Very resistant to pests.*	*Experience of growing this species in commercial plantations in NSW is evolving, and only limited good quality genetically improved seed available.*	*Should perform well, and provides a FEA with a strong back-up species for E dunnii.*

** CCV is Corymbia citriodora variety variegata.*

Summary of FEA plantations

FEA's eucalypt plantations in Tasmania are among the finest in Australia. With an excellent species, 20 years of experience in site acquisition and silviculture plus good supporting technical information, the existing situation provides an excellent basis for the 2008 Project. Similarly, there are decades of experience and strong supporting data to underpin the expansion by FEA into radiata plantations.

Pest control

FEA is a pioneer of commercial hardwood plantation forestry in northern NSW. The early plantations were variable in terms of growth and health and it was necessary for FEA foresters to resolve a number of issues relating to species, sites and pest and weed control. The early plantations were not able to use high quality genetically improved seed, as it was not available. Good progress has been made.

However, compared with eucalypt plantation forestry in Tasmania, the methodology and technology in the subtropical regions is still evolving. Pest control is absolutely critical, with E dunnii being vulnerable to defoliation by Pysillids and spotted gum being deformed by the fungal pathogen Quambalaria.

Yield

There are no mature eucalypt pulpwood plantations in the region with comparable species and silviculture, and a paucity of trial plots which can be measured to verify predictions of growth and yield. FEA does not yet have growth curves or yield tables for any of the species being planted in NSW/Qld but is working on these areas. Estimates of yield are projections from measurements of immature plantations, or are based on growth rates for similar species measured overseas, and computer models.

Although there has been a long established forest industry based on native forests in northern NSW and southeastern Qld, there is no existing pulpwood industry, apart from the export of softwood chips from Brisbane. FEA is able to describe a likely scenario for their plantations in which thinnings are converted into woodchips using mobile chippers 'on site' and then taken to Brisbane Port by rail or truck, and sawlogs are processed in a new FEA sawmill and timber processing facility to be built in the region. This will be capable of producing high quality hardwood sawn timber from small logs, as currently exists at Bell Bay, and also processing residue material either into export quality woodchips, or some other material for sale into the domestic market. Likely and highly suitable sites for a mill have been identified near Casino, and FEA has experienced specialist staff working on this development.

The Consultant Forester does not foresee any major obstacles to this scenario; the issue is simply getting the basic work done to set it all up. Fortunately, well before plantations in the 2008 Project reach the age for first thinning, FEA will have nine years in which to plan and implement the approach to harvesting, processing and marketing for the NSW/Queensland region. Furthermore, there is a significant existing plantation resource in the region arising from earlier FEA projects plus other private and government plantings, some of which FEA has recently acquired. These will all need to be harvested, transported, processed and marketed well ahead of any plantations established in the 2008 Project.

9.5. Operational Management

Staff

FEA is managing complex forest growing, harvesting, timber processing and marketing operations in three States in eastern Australia. Sustainable commercial success demands high standards of corporate governance, strategic planning, field operations, technical services, administration and marketing and for a high level of leadership to keep the whole operation moving forward positively.

The Consultant Forester is satisfied that FEA have the staff to meet these demands. A major expansion of operational and specialist staff has occurred in NSW and Queensland over the last 18 months. This was needed to cope with the rate of plantation expansion in this region and with the need to develop harvesting, marketing, export and processing systems.

Currently FEA has a high quality and dedicated team responsible for forestry operations, with a good blend of older experienced and energetic younger men and women. The Consultant Forester was impressed with the high level of esprit de corps and the determination to do a good job amongst FEA personnel.

Two issues are raised: (i) there is an urgent need for two full-time dedicated research scientists on the staff and located in NSW, focussing on weed and pest management and nutrition; and (ii) there is a need for FEA to assign resources to establishing seed orchards of the four main species being planted by FEA in NSW similar to the excellent work they have done with E nitens in Tasmania.

These issues have been raised with FEA and they advise that they will be applying resources to these issues in the near future.

Field visit

The consultant visited Tasmania (November 2007) and Northern NSW (January 2008) before preparing this report, and made a detailed inspection of a range of FEA plantations, met with FEA field staff, and examined the Bell Bay sawmill.

Management and Operational Capability

This project is FEA's sixteenth consecutive MIS eucalypt forestry project. This demonstrates FEA's capacity to successfully develop and implement forestry projects. As with previous projects, FEA intends to carry out the forestry operations in the field utilising their forestry staff located in NSW and Tasmania, and using contractors for various roles, under the direction of the leadership group located in Launceston, Tasmania, and the regional office in Lismore, NSW.

FEA has a high level of professional leadership. CEO Andrew White is a forester by training, and has wide experience in the timber industry and in the business world. The company's Director of Forestry Services and the Chairman of the Responsible Entity for the Project is Tony Cannon, one of Australia's most experienced and respected plantation foresters. The General Manager of Plantations is Chris Barnes who is an agronomist by training and who has extensive experience in forest research and operations and in project management.

FEA is a maturing organisation and is today regarded as one of the most experienced and professional players in the Australian forestry and timber industry scene. Originally their plantation operations were all within Tasmania, but FEA has been operating on the mainland in NSW and Queensland since 2001and have staff permanently located in this region. During the last two years, FEA has significantly expanded their resources in NSW, with appointments of managerial and specialist staff.

FEA has established good working relationships with State forestry agencies, and also with the Southern Cross University at Lismore. FEA has access to experienced consultants in the fields of timber processing, harvesting, marketing and export. FEA is a member of the CRC for Forestry and the Subtropical Forest Health Alliance.

FEA is fully accredited to ISO 14001:2004 and has in place an Environmental Management System audited by a third party. All of the forestry operations in Tasmania are certified by the Australian Forestry Standard (AFS). FEA is currently working towards certification under the Australian Forestry Standard for plantation operations in NSW and Qld. FEA advise that this is likely to be achieved by mid-2008, and if this occurs, the 2008 Project will be fully certified.

FEA's total plantation area under management is over 50,000 hectares in three states. FEA has a joint venture arrangement with ITC (ITC is a major shareholder in FEA) for the marketing of SmartFibre (woodchips) in Japan. The JV entity is SmartFibre Pty Ltd (SmartFibre).

This arrangement enables FEA to be a partner in a sustainable woodchip production operation and to maximise prices and market share.

9.6. Project Review

Twelve critical factors need to be satisfied if this project is to be a success in terms of a commercial plantation project. These are listed, together with the Consultant Forester's comments on the degree to which they are recognised and dealt with in this project by FEA Limited and FEA Plantations Limited in Table 9.1 below.

Table 9.1 Summary of critical factors and comments

Factor	Consultant Forester's comments
The site selected must be suitable for the species to be planted.	*Land in both Tasmania and NSW/Queensland which is similar to that acquired by FEA in the past and likely to be acquired in the future were inspected, including some land likely to be used for the 2008 Project.* *The Consultant Forester reviewed the land acquisition protocol set out by FEA and endorsed by their Independent Forester and this was found to be sound. It has clearly evolved in the light of experience over recent years. The staff responsible for land acquisition on the mainland were found to be competent and responsible, giving confidence that suitable land will be acquired for the 2008 Project.*
The right species must be planted for the sites, and these should have timber qualities which match intended end use.	*FEA will be planting E nitens in Tasmania and the tablelands area of NSW and principally spotted gum (CCV) and Dunn's white gum in NSW/Queensland. Sydney blue gum will also be planted on some sites. Nitens, spotted gum and Sydney blue gum are all appropriate in terms of both the environment and the marketplace. E dunnii has been shown in research studies to have potential value as sawn timber, even unpruned, provided it is properly dried. Spotted gum (while it produces good quality pulp) is not currently a widely used pulpwood species and will require specific marketing. Both of these issues should have been resolved before the 2008 Project matures. P. radiata will be planted in Tasmania.*

Environmental and legal approvals must be in place, and conditions built into all forestry prescriptions, and a control system put in place.	*Approvals processes are well understood by FEA and have been implemented in the past without problem. FEA's environmental management system is accredited under ISO14001 and the woodchip export business meets the Controlled Wood Standards of the FSC. All plantation operations in Tasmania are certified under the Australian Forestry Standard, and this is likely to be extended to the mainland operations in 2008. FEA is aware of the need to meet legal requirements. One of their field staff in NSW is a lawyer and very experienced in the various legal and environmental issues associated with plantation development. FEA do not intend to clear any native forest for plantation establishment, other than as approved by government authorities.*
Genetically improved seed of a known and suitable provenance must be used.	*FEA is using the highest quality genetically improved seed for E nitens and E dunnii that they can acquire. In the case of nitens, this is good quality, seed orchard seed, including seed of the Northern Provenance for planting in NSW. In the case of spotted gum it is imperative that the Richmond Range provenance be used, as this is less susceptible to Quambalaria attack. Access to quantities of seed of this provenance is difficult, and some other provenances will have to be planted with consequent higher risk. FEA has its own E nitens seed orchard established, and some seed from this has already been collected and will be available for part of the 2008 project.*
A capable nursery must be used to produce quality seedlings.	*FEA uses several contract nurseries. One of these was inspected and found it to be excellent. The Consultant Forester also inspected seedlings in other areas planted as part of the 2006 Project and generally found them to be of a good standard.*
Planning, site preparation and follow-up is required to ensure efficient and successful establishment.	*FEA employs a well-tried methodology of site preparation, involving 'clean-up', access roads, initial weed control, ripping and mounding or spot cultivation for second rotation sites, secondary weed control and planting. Follow-up survival counts and replanting is carried out to meet an objective of 90% survival at age 1.*
Effective weed control is essential	*This is understood by FEA, but it is not always possible in NSW/Qld where adverse weather conditions (heavy summer rain) can delay operations. Close attention is needed to this aspect of the work, a need recognised by FEA.*
Nutrition must be managed across the rotation.	*Nutritional management on the sites being used in this Project is not as critical as for some plantation projects elsewhere in Australia, as the sites being planted are fertile. Some sites in NSW/Queensland will require additional fertiliser during the rotation; monitoring and research are essential. FEA has established some fertiliser trials on their earlier plantations and have demonstrated that they will use fertiliser when required, for example treating a stand in NSW for boron deficiency. FEA advise that the company is well aware of the linkage between good nutrition and pest resistance. However, there is a need for a dedicated researcher to work on nutritional management in NSW, especially in relation to the interaction between weeds, fertiliser and tree health.*
Pest management	*All of the eucalypts to be used in this project are subject to insect and fungal pests to some degree, although Sydney blue gum has few problems to date. E nitens in Tasmania can suffer from infestation with Chrysomelid beetles, E dunnii in NSW/Queensland from Pysillids and CCV from the fungus Quambalaria. E dunnii can also be attacked by the Giant Wood Moth, especially if the trees are already weakened by Psyllid attack. Chrysomelids and Pysillids can be controlled by aerial spraying with pesticides. In the case of dunnii, this is essential. Operations need to be timely, and good monitoring is essential. FEA has evolved adequate systems for monitoring and control operations over the last three years and this has lessened a potentially project-threatening risk. FEA is also increasingly using E saligna in place of E dunnii, and the former is a significantly more pest-resistant species.*

Bushfire management	*Bushfire management is required for all plantations in Australia. Although the climate in NSW/Queensland and northern Tasmania is less conducive to frequent fires, fires can still occur. In Tasmania FEA has extensive experience in bushfire management and has cooperative arrangements in place with other forestry organisations and bushfire brigades. All FEA field staff are trained to basic competencies as firefighters. In Queensland and northern NSW the company is also using cattle to graze fuels in the older plantations, to good effect. A critical time will be immediately after pulpwood thinning, when fuel loads within the plantations will be high. There is nothing that can be done to ameliorate this, and the need for growers to have insurance is supported.*
Research and inventory systems must parallel operational work.	*FEA has a sound inventory program in place in Tasmania and has appointed an inventory specialist to develop new systems for NSW/Qld. This work is critical.* *Until recently FEA has not developed its own forestry research arm, but has relied upon a consultant to undertake genetics research with E nitens, and collaborative arrangements with external agencies and CRCs to carry out research. FEA now recognise the need for in-house research into genetics, silviculture and nutrition (especially in NSW) and has appointed one person to work in this area. This is not adequate. Two further key research needs are operational control measures for Quambalaria attack on spotted gum and the advancement of the new spotted gum hybrids, which are highly pest-resistant. FEA needs to consider the appointment of additional research staff.*
Organisational capability	*FEA has a combination of professional skills and youthful energy, supported by an experienced Board. The Consultant Forester feels confident they will be able to take this project through to maturity and to provide the supporting systems around it to ensure it works. FEA has significantly built up their managerial and forestry staff and supporting systems (including processing and marketing) in NSW/Queensland. The most critical element will be the ability over time to manage a widely dispersed estate and to maintain standards across a wide area – a problem which is faced by most expanding Australian plantation companies.*

9.7. Conclusions

This review of the FEA Plantations 2008 Project and the recent inspection of operations in Tasmania and NSW/Queensland have led to the following conclusions:

1. *FEA is a relatively small, but growing forestry company, and has earned a respected place in the Australian forestry and timber industry. The Consultant Forester regards FEA as a responsible and professional forestry organisation, with the added advantage of being vertically integrated and well established into processing and export. The Consultant Forester is confident that FEA's field staff will do their best to make this project a success, and approves of the fact that there is a system in place for internal audit via FEA Plantations.*
2. *FEA has made significant advances in management of the mainland operations over the last 2 years, and is already addressing critical processing and marketing arrangements.*
3. *FEA's pioneering developments in processing small sawlogs into EcoAsh® are impressive. This is a good product, well presented, and capable of being further refined in the light of FEA's timber engineering research. FEA has evolved a neatly integrated system from stump to marketplace, where value is being added and waste minimised at each step. Growers in this project will benefit from this if, as anticipated, a higher volume of sawlogs are recovered than currently projected and higher stumpage prices eventuate.*
4. *The expansion into NSW/Queensland has involved several years of pioneering and trial and error. The early plantations are unlikely to meet expectations but will definitely produce volumes of saleable timber, and have provided FEA with a solid base of experience. This will allow FEA to refine its silvicultural, harvesting, processing and marketing systems in this region well before the 2008 Project matures. The exploratory phase has now largely been worked through, but there are still refinements to be made, especially with respect to genetics, nutrition and weed and pest control. An expanded use of E saligna in lieu of E dunnii is supported.*

5. *The projected yields for Project 2008 plantings in Tasmania may be marginally optimistic but are not unrealistic for stands being grown on to age 13 and 16. Yields cannot be verified for NSW/Queensland as there is insufficient supporting data. To achieve projected yields across the whole project, it will be necessary for the NSW/Queensland plantations to perform well, and this in turn will call for intensive control of weeds and pests and improved nutritional management. It is considered essential that FEA invest further resources in research into these aspects.*

6. *The estimates of projected stumpages and of sawlog margin are considered to be marginally conservative.*

The Consultant Forester concludes that the project can be supported from a forestry viewpoint, provided FEA continue to expand their investment in research and development for the mainland plantations.

10. Application of Funds and Ongoing Costs

10.1. Growers' Establishment and Ongoing Fees

Details of grower fees are provided in section 7 of the PDS and summarised further in section 4 (Investment Offer and Structure) of this report.

10.2. Manager Revenues, Costs and Profit

Lonsec has reviewed the cash flow model provided by the RE and has extracted the following revenue and cost information, excluding GST. The costs are the cumulative totals cost for the life of the Project and include the effect of inflation.

Table 10.1 Grower Payments

Grower Payments	Option 1		Option 2		Option 3		Option 4	
	$/ha	% of Total	$/ha	% of Total	$/ha	% of Total	$/ha	% of Total
Establishment Fee	6,300	71%	6,300	43%	6,300	59%	6,000	60%
Pruning Fees	-	-	2,695	18%	-	-	385	4%
Deferred Lease and Management Fee	2,594	29%	5,635	39%	4,367	44%	3,535	36%
Total	**$8,894**	**100%**	**$14,630**	**100%**	**$10,667**	**100%**	**$9,920**	**100%**

Table 10.2 Manager Costs

Manager Costs	Option 1		Option 2		Option 3		Option 4	
	$/ha	% of Total	$/ha	% of Total	$/ha	% of Total	$/ha	% of Total
Preparation & Planting Costs	2,872	32%	2,667	18%	2,667	25%	2,784	28%
Lease Costs	3,492	39%	4,254	29%	4,506	42%	3,890	39%
Maintenance Costs	802	9%	1,233	8%	2,027	19%	1,213	12%
Pruning Costs	-	-	2,079	14%	-	-	297	3%
Forestry Expenditure	***$7,166***	***81%***	***$10,233***	***70%***	***$9,200***	***86%***	***$8,185***	***83%***
Overheads & Management	400	4%	400	3%	400	4%	400	4%
Commissions & allowances	630	7%	630	4%	630	6%	600	6%
Manager Tax paid	210	2%	1,010	7%	131	1%	220	2%
Manager Profit after tax	489	6%	2,357	16%	306	3%	514	5%
Total Non-Forestry Costs	**$1,729**	**19%**	**$4,397**	**30%**	**$1,467**	**14%**	**$1,735**	**17%**
Total	**$8,894**	**100%**	**$14,630**	**100%**	**$10,667**	**100%**	**$9,920**	**100%**

As shown in Table 10.2 above, Forestry Expenditure is equal to or exceeds 70% in Options 1, 2, 3 and 4.

On the basis of these figures FEA Plantations will generate after tax profit margins of 6% for Option 1, 16% for Option 2, 3% for Option 3 and 5% for Option 4.

Growers must be aware that these returns are calculated on an accounting basis, which does not take account of the time value of money and so cannot be compared directly with the after tax IRR earned by the Growers.

Ideally, the Grower IRR would be compared with the Manager IRR, but it is not always possible to calculate the IRR of a given cash flow, as the ability to make the calculation depends on the specific timing of the cash inflows and the cash outflows. The Manager cash flow as assessed by Lonsec falls into this category.

However, another method of comparison is available, wherein the net present values (NPV) of the Grower and the Manager cash flows, discounted at a common rate, can be compared in magnitude. Lonsec has performed such a calculation, in this instance discounting both the Grower and Manager cash flows (consolidated FEA and FEA Plantations) at the Grower IRR.

The result will always be a zero NPV for the Grower (the IRR of a cash flow is, by definition, the discount rate that returns a zero NPV) which can be compared with the NPV of the Manager cash flow. The results of the NPV analysis of the Manager's after-tax cash flow is provided in table 10.3 below.

Table 10.3 After-tax NPV Analysis

	Option 1	Option 2	Option 3	Option 4
Grower IRR	8.5%	9.1%	8.0%	8.8%
FEA NPV at Grower IRR	$730	$645	$516	$94
FEA NPV at nominal rate (10%)	$779	$700	$645	$127

This analysis would tend to indicate that returns from the Project may be skewed toward the Grower. This is consistent with the relatively low after-tax returns to the Manager shown in Table 10.2 above. However, what is not clear is the extent to which (in any) there are profit margins in the cost items shown in Table 10.2.

11. Product Disclosure Statement Assumptions

11.1. Financial Model and Directors' Assumptions

The Responsible Entity has sought opinion on key project assumptions from experienced industry consultants in their fields of expertise, including woodlot yields, future timber trends, and future costs.

Lonsec's assessment of key project assumptions is based on the expert advice of the Lonsec Consultant Forester, the PDS Expert Reports and benchmarking to verifiable industry benchmarks and historical results.

Lonsec has stated its reasonable range for each key assumption, and note that the likelihood of any long term assumption (greater than two years) being achieved varies inversely with the time period projected.

Growers should be aware that unforeseen circumstances could impact on the stated assumptions in the PDS. It is important to recognise that long range returns will be based on economic, physical, and environmental inputs that are impossible to predict with accuracy.

Specific quotations from the Lonsec Consultant Forester's Report are identified in italics.

11.2. Woodlot Yield

The Lonsec Consultant Forester's comments on yield are as follows:

The Consultant Forester has reviewed the projected yields and product mix for E nitens in Tasmania. An MAI of 27 is forecast. The Consultant Forester has also studied the growth curves developed by FEA for E nitens from their existing plantations and computer modelling of projected growth for E nitens and other species based on early growth. As a consequence a projected MAI of 27 is seen as achievable for 13 and 16-year rotation lengths, but slightly at the high end of expectations. Projections for NSW/Qld are theoretical, and are completely dependent on successful control of insect and fungal pests.

On the other hand, the recovery of sawlogs may be higher than the expected product mix quoted by FEA in the PDS. The recovery of sawn timber from sawlogs may also be higher than is presently being achieved, due to superior milling and drying technology. The higher return from a higher recovery of sawlogs would counteract any small shortfall in yield.

FEA's yield projections for radiata pine plantations are reasonable and supported by long experience with this species in southern Australia.

11.3. Price

Lonsec calculates stumpage prices for specific locations, having regard to the woodchip price specific to that location (or an imputed woodchip price recognising differences in sailing distances from that location to the destination port) with adjustments, if necessary, for wood density, pulp yield and the specific costs for roading, harvesting, transport, chipping and loading at that location.

FEA has assumed eucalypt stumpage prices of $42.00/m^3 at thinning and $45.00/m^3 at clearfall, based on the current Bell Bay plantation woodchip price of $198.50/BDMT.

However, Bell Bay plantation woodchip prices have risen significantly over the past few years and are now well above the long-term trend. Lonsec has assumed a lower Bell Bay plantation woodchip price of $189.77/BDMT, escalating at 2.6% pa for the life of the Project. This leads to eucalypt stumpage prices of $38.00/m^3 at thinning and $41.00/m^3 at clearfall.

The Lonsec Consultant Forester's comments on price are as follows:

It is virtually impossible to project the price of an internationally traded product ten years hence. It seems highly likely that eucalypt plantation woodchips will still be in increasing demand in ten years time and that Australia will be one of the world's leading suppliers. Unless there is a major change in exchange rates, prices will remain steady. In fact, movements in exchange rates for some competing chip exporting countries like South Africa and Chile will favour Australian woodchip producers. To this extent current prices are a reasonable indicator of future prices.

FEA has three factors in its favour for this project with respect to woodchip prices: (i) the advent of the Gunns Pulpmill at Bells Bay will benefit FEA either directly or indirectly; (ii) woodchip exported from Brisbane will enjoy a shipping advantage and will be a more valuable product because of its lower moisture content; and (iii) FEA has developed the "certified" SmartFibre product, which it will market with ITC, thus producing a higher volume of quality material, for which a higher price should be achieved.

The solid wood products produced in this project will go to FEA's Optimil sawmill, or to a new sawmill to be built in NSW. Or it may go as veneer logs, either to the domestic or the overseas market. Under the Wood Purchase Agreement between FEA and FEA Plantations, growers are assured that FEA will purchase the wood from thinnings and final harvest, and will pay a "fair and reasonable price". An important issue is the fate of high quality pruned logs which could be used by FEA in their sawmill for production of EcoAsh®, but which may fetch a higher price as veneer logs exported to (for example) China or used by domestic veneer mills. The Consultant Forester's understanding is that FEA's offer is a right of first refusal, with the price independently signed-off before FEA Plantations can accept it.

If FEA Plantations receives a better price offer for the logs (under similar terms and conditions) then FEA can choose to match that price or not. If they opt not to match it FEA Plantations is free to sell to the alternative buyer. This is fair to the Grower.

The stumpage estimates set out by FEA are reasonable, indeed may be marginally conservative.

11.4. Exchange Rates

Growers may be exposed to exchange rate risks. The price offered by Purchasers may be subject to export market conditions where revenues are received in foreign currencies.

11.5. Price and Cost Inflation

Lonsec has the view that it is appropriate to assume a long term Australian inflation rate (CPI) of 2.6%. This view is based on a RBA survey of market economists for the year to June 2009.

11.6. Costs

Detailed costs are tabulated in Section 10 Application of Funds and Ongoing Costs. The Lonsec Consultant Forester's comments on costs are as follows:

The Consultant Forester has inspected a cost schedule for establishment and maintenance provided by FEA for this project, and a range of operations on the ground. The Consultant Forester has concluded as follows:

- *Plantation forestry with E nitens in Tasmania currently follows a uniform pattern and the cost components are well established for the different sites, whether or not the new plantation is first rotation or second rotation. FEA's costs should not be different from those of other plantation managers.*
- *Plantation forestry in the sub-tropics, (NSW/Queensland) is inherently more expensive than that in southern Australia, mainly due to the demands for weed and insect control, although to some extent this is offset by having larger areas (and economies of scale) compared to Tasmania, and the lack of need to control browsing animals.*

On balance, it is reasonable to expect that the operational costs for FEA's plantation operations should be on a par with those of other forestry organisations.

11.7. Summary of Assumptions

Table 11.1 Summary of Key Assumptions

Assumption	Units	Low Case	Mid Case	High Case
Cost Inflation	% pa	3.0	2.6	2.0
Price Inflation	% pa	2.0	2.6	3.0
Option 1				
MAI	m^3/ha/yr	22	27	32
Stumpage Price – pulpwood (thinning)	$/$m^3$	33.35	38.00	41.80
Stumpage Price – pulpwood (harvest)	$/$m^3$	37.16	41.00	45.10
Stumpage Price – sawlog (thinning)	$/$m^3$	40.02	46.88	51.56
Stumpage Price – sawlog (harvest)	$/$m^3$	44.59	50.63	55.69
After Tax IRR		**4.8%**	**8.5%**	**10.7%**
Option 2				
MAI	m^3/ha/yr	22	27	32
Stumpage Price – pulpwood (thinning)	$/$m^3$	33.35	38.00	41.80
Stumpage Price – pulpwood (harvest)	$/$m^3$	37.16	41.00	45.10
Stumpage Price – sawlog (thinning)	$/$m^3$	40.02	46.88	51.56
Stumpage Price – sawlog (harvest)	$/$m^3$	62.43	81.00	89.10
After Tax IRR		**5.7%**	**9.1%**	**11.7%**
Option 3				
MAI	m^3/ha/yr	20	22	24
Stumpage Price – pulpwood	$/$m^3$	9.40	11.00	12.10
Stumpage Price – small sawlog	$/$m^3$	25.00	29.40	32.30
Stumpage Price – medium sawlog	$/$m^3$	41.10	48.20	53.00
Stumpage Price – large sawlog	$/$m^3$	58.30	68.60	75.50
Stumpage Price – extra large sawlog	$/$m^3$	46.30	80.30	88.40
After Tax IRR		**6.2%**	**8.0%**	**9.2%**
Option 4				
After Tax IRR		**6.7%**	**8.8%**	**10.6%**

FEA has entered into a Wood Purchase Agreement with FEA Plantations as agent for the Growers.

Growers in Woodlot Options 1 and 2 will have the benefit of a Floor Price mechanism, provided for in the Wood Purchase Agreement. The Floor Price mechanism provides that FEA will pay Growers the greater of either the prevailing market price at the time of harvest or the price determined by applying the Floor Price mechanism.

The Floor Price mechanism does not apply to Option 3 (Radiata Pine) but it does apply to the Option 1 and 2 components in Option 4.

Table 11.2 below shows the method by which Floor Prices are determined.

Table 11.2 Determination of Floor Prices

Product	Thinning	Clearfall
Option 1		
Pulpwood	0.35 X FOB Bell Bay Price	0.39 X FOB Bell Bay Price
Sawlog - Unpruned	1.2 X Pulpwood Floor Price at thinning	1.2 X Pulpwood Floor Price at clearfall
Option 2		
Pulpwood	0.35 X FOB Bell Bay Price	0.39 X FOB Bell Bay Price
Sawlog - Unpruned	1.2 X Pulpwood Floor Price at thinning	1.2 X Pulpwood Floor Price at clearfall
Sawlog - Pruned	n/a	2.0 X Pulpwood Floor Price at clearfall

12. Risks and Risk Management

12.1. Lonsec Risk Assessment

Growers need to be aware that the investment contains risks inherent to all long term commercial forestry projects, risks particular to plantations, financial risks and other risks. Section 7 of the PDS outlines a range of risks specific to the Project and FEA Plantations' management procedures in dealing with these risks. Growers should read and understand these issues before investing in this Project.

The Lonsec analysis of risks aims to assess the degree of Project risks within five categories from Low to Extreme.

The formulation of the overall risk category is a combination of analysis including:

- Lonsec Determinant Ratings Analysis – incorporating qualitative and quantitative assessment criteria.
- Lonsec Consultant Forester's Opinion – detailing specific risks associated with forestry operations.
- Risk Profile Table – includes an assessment of the likelihood, consequence, and management of risks.
- PDS and Project Expert Reports – a review of the information provided by project management.

Lonsec has rated Option 1, 2, 3 and 4 of the FEA Plantations Project 2008 in the "**Moderate"** risk category.

	Low	Moderate	High	Severe
Option 1				
Option 2				
Option 3				
Option 4				

12.2. Principal Forestry Risks

The Lonsec Consultant Forester's comments on forestry risks are as follows:

Weed and pest management in the sub-tropics

As discussed above, plantation growing in the temperate area of Tasmania can now follow well-tried and tested procedures, but the job in NSW/Queensland is more difficult and requires a different emphasis.

Failed weed and pest control are the most serious threats to the project. To a large extent this is in the hands of FEA. Considerable progress has been made in the last 2 years, especially in respect to control of Pysillids on E dunnii. This species will not develop into a satisfactory plantation if Psyllid defoliation is not prevented. Similarly good management of weeds and nutrition is needed to minimise the Quambalaria problem with spotted gum, and it is noted that FEA staff are aware of this. This consultant would like to see proactive field studies by FEA into measures for controlling Quambalaria as well as into optimising the inherent capacity of spotted gum to resist its attack.

The technology of weed management is well known, and FEA has been a leader in this area. The key requirement is for timely action, using established methodology.

Fire

The risk of fire in plantations is ever present, and is recognised by FEA. There is a requirement to ensure their plantations are responsibly provided with firebreaks and that staff are well trained, and have developed or are developing a fire response capability.

The Forestry Consultant believes that FEA are well prepared in Tasmania and will be able to handle everything apart from a regional bushfire disaster (of which there has been only one in Tasmania in the last 50 years, and this was in southern Tasmania, where FEA has only a tiny proportion of its plantation estate). The situation is more complex in NSW/Queensland, where the plantation estate is highly fragmented and scattered over hundreds of kilometres. Fragmentation has the advantage of reducing the risk of a single fire causing extensive damage, but the disadvantage of increasing the time and effectiveness of response to a new fire. The key requirement here is therefore fuel management within the plantation to mitigate potential fire damage. FEA have been using cattle grazing for this purpose in most plantations and this is effective in reducing grassy fuels. This should become routine.

Nevertheless it will be prudent for investors in this project to take out fire insurance, as no guarantee of freedom from fire can ever be given.

Projected yields and product mix

FEA is able to confidently predict yields and product mix for Option 1 and Option 2 schemes with E nitens in Tasmania. The Forestry Consultant has reviewed this data and finds it credible.

There is a small risk that there will be a loss in dominance of pruned trees within an unthinned stand. For Option 2 plantations, FEA will be pruning 450 Final Crop trees per hectare at about ages 2-6 within a stand carrying 1200 trees to the hectare, but thinning is not scheduled until age 9. Where pruning takes off live branches and more than half the live crown is removed at any time, the growth rate of the pruned trees will often decline relative to neighbouring unpruned trees. FEA advise that pruning will be carried out by experienced contractors, and will be well supervised and do not expect these problems to arise.

Project yields and product mix for stands grown in NSW/Qld are not yet supported by actual data from mature plantations, and it will be 3-4 years before sound estimates can be made. Early inventory demonstrates that provided weed and pest control is effective, yield expectations are likely to be achieved. It is pleasing to note the emphasis FEA is putting into research into this area.

Political issues

There is a negative attitude to plantations amongst some Tasmanian environmentalists. This is based on two main concerns: the need to control native browsing species at the time of plantation establishment to ensure the new tree seedlings survive, and conversion of native forests to plantations. The latter concern is not realistic, as FEA do not intend to replace native forests with plantations, but will be planting either on newly acquired farmland, or onto sites which already carry plantations.

The main browsers are possums and two species of wallaby. If they are not controlled, they move into the plantations and eat the newly planted seedlings. They are controlled mainly by shooting, poisoning or trapping. This is needed for about one year after planting, after which the small trees become tall enough to escape browsing, and control operations cease.

Concerns about animal control are not warranted. The possum and wallaby species are abundant and their numbers recover quickly when control measures cease. Furthermore, FEA has developed a form of seedling "guard" which is already proving effective, and there are research programs leading to a reduced need for control in the future (including planting for this Project).

12.3. Other Risks

Changes in the law

Growers should be aware that the success of the Project and the returns achieved by Growers may be affected by changes in the taxation, regulatory, or legal environment, including changes in legislation and the imposition of new levies, imposts or other taxes.

Project agreements

Anything that affects FEA Plantation's ability to meet its obligations under the Constitution of the Project, the Sub-contracting Agreements, the Management Agreement, Forestry Right Deeds and the Wood Purchase Agreement constitutes a risk to Growers.

Loss of key staff

Loss of key staff with the necessary forestry skills can be a major problem, especially where intensive forestry management systems are employed. FEA's on-going training programs for permanent staff and awareness of this issue should be sufficient to address this risk.

12.4. Risk Profile Table

Lonsec has listed in Table 12.1 the critical Project risks, the potential impact and the level of risk management that is expected to be achieved.

The tabulation shown is based on Standards Australia Risk Management Standard AS/NZS 4360:1999.

The five most critical risks facing the project have been assessed as follows:

1. Growth rates lower than expected
2. Timber price lower than expected

3. Market demand lower than expected
4. Loss of key staff
5. Changes in substance or interpretation of applicable laws relating to Income Tax, GST, environmental matters, native title

12.5. Risk Management

Insurance

FEAP will arrange for insurance in its name and the names of the Growers against public liability arising out of the use of the Project land no less than $10,000,000. FEAP will pay for the cost of public liability insurance.

Growers can apply for one of two different levels of insurance.

- *Basic Insurance* – insures against loss of trees due to fire, wind or hail damage. This is optional if not obtaining finance from FEA.
- *Full Replacement Cost Insurance* – insures the Grower's interest for the original amount invested until the value of the interest exceeds the value of the initial investment. This level of insurance is compulsory for Growers who obtain finance from FEA, for longer than one year, and must be maintained during the full term of the loan.

If requested in writing, FEA Plantations will use its best endeavours to arrange insurance requested by Growers. FEA Plantations will determine the cost of insurance on an annual basis and will invoice Growers for the cost of insurance (inc. GST) plus a 10% administration fee.

Stocking Guarantee

Any trees destroyed for any reason in the first year after planting will be replanted by FEA Plantations to 90% of the initial planting density (600 seedlings per hardwood Woodlot) as practicable at no additional cost to the Grower.

Limitation of Grower's Liability

The Grower's liability is limited to the amount paid, or agreed to be paid for an interest in the Project.

Table 12.1 Lonsec Risk Profile Table

FEA Woodlot Project 2008		Lonsec's AS/NZS Based Risk Assessment			
		Likelihood Rating	**Consequence Rating**	**Proportion of risk expected to be managed**	**Net Level of Risk**
Description of Risk	**Possible Outcome**	Rare Unlikely Moderate Likely Almost certain	Insignificent Minor Moderate Major Catastrophic	 Low Moderate Major High	5 = Low 10 = Moderate 15 = High 20 = Severe 25 = Extreme
Forestry Risks					
Growth rates lower than expected	Volume of timber reduced, revenue reduced	Moderate	Major	Moderate	9
Trees destroyed or damaged by drought	Timber yield reduced	Unlikely	Major	Major	4
Trees destroyed or damaged by wind	Timber yield reduced	Unlikely	Moderate	Major	3
Trees destroyed or damaged by fire	Timber yield and quality reduced	Unlikely	Major	High	2
Trees destroyed or damaged by pests or disease	Timber yield and quality reduced	Unlikely	Major	Major	4
Management Risks					
Loss of key staff	Skills, experience and intellectual property, management may be compromised	Moderate	Moderate	Major	5
Failure of Responsible Entity or withdrawal of Licence	RE can be replaced, possible delay in bringing in new Growers	Rare	Major	Major	2
Failure to achieve Minimum Subscription	Project does not proceed. Fees are refunded but investment opportunity would be lost	Rare	Minor	Major	1
Marketing Risks					
Market demand lower than expected	Volume of timber sold reduced, price possibly weakened, revenue reduced	Moderate	Major	Moderate	7
Timber price lower than expected	Revenue reduced	Moderate	Major	Moderate	7
Other Project Risks					
Changes in substance or interpretation of applicable laws relating to Income Tax, GST, environmental matters, native title	Adverse financial impact on Members	Moderate	Moderate	Major	5
Insufficient land available to allow establishment of project at desired size	Economies of scale not achieved for Growers and Forestry Manager	Moderate	Moderate	High	2
Fluctuations in exchange rates	Timber price expressed in A$ could decrease	Moderate	Moderate	Major	5
Supporting infrastructure	Loss of facilities to harvest, transport and process the timber, and sell the timber	Rare	Moderate	Major	2

13. Financial Returns

13.1. Investment Cash Flow

The focus of the Lonsec financial performance measure is defined by the Internal Rate of Return (IRR) of the Project and related model sensitivities. Whilst not a holistic measure of project performance, the IRR analysis generates a single number that summarises the merits of an investment based on the cash flows. The IRR is compared with Lonsec benchmarks. In order to comply with ASIC guidelines, the PDS does not have IRR estimations.

It is important to recognise that the Lonsec IRR estimates disclosed below should not be used as a basis for an investment decision by potential Growers. The Lonsec possible IRR outcomes are simply an assessment by Lonsec that the Project meets industry and Lonsec benchmarks, and is limited by typical uncertainty of long term forecasts.

There is a considerable degree of judgement involved in making long-term forecasts, and future outcomes may differ substantially from the Lonsec IRR estimates. Lonsec also examines the sensitivity of the Project to varying assumptions which identifies those key variables which have the most sensitive correlation to potential Project returns. Lonsec strongly advises Growers and financial planners to simulate their own long term financial projections using their own selected assumptions to provide a basis for investment decision making. This is in line with current ASIC guidelines.

13.2. Financial Returns and Scenario Modelling

Lonsec has modelled a number of scenarios, based on ungeared mid case assumptions, to reflect the impact on the Project returns of varying the key assumptions. The results are provided in Table 13.1 below.

Table 13.1 Mid Case Returns and Scenario Modeling

Parameter	Scenario	After Tax IRR (ungeared)			
		Option 1	Option 2	Option 3	Option 4
Stumpage Price ($/m^3)	Price High Case	9.3%	9.9%	8.4%	9.3%
MAI (m^3/ha/yr)	MAI High Case	9.3%	9.9%	8.4%	9.3%
Price Inflation	Price Inflation High Case	8.9%	9.6%	8.4%	9.1%
Cost Inflation	Cost Inflation Low Case	8.5%	9.2%	8.0%	8.8%
Mid Case Assumptions		**8.5%**	**9.1%**	**8.0%**	**8.8%**
Cost Inflation	Cost Inflation High Case	8.5%	9.1%	8.0%	8.8%
Price Inflation	Price Inflation Low Case	7.8%	8.5%	7.3%	8.4%
MAI (m^3/ha/yr)	MAI Low Case	6.8%	7.6%	7.5%	7.8%
Stumpage Price ($/m^3)	Price Low Case	7.4%	8.2%	7.2%	8.0%
Insurance	Basic Level	8.1%	8.9%	7.7%	8.5%

Option 1 Returns

The scenario modelling shows that the financial returns vary between 6.8% and 9.3%. The IRR based on mid case assumptions is 8.5% and occurs at the mid point of the Lonsec benchmark range for pulpwood projects.

The Project is expected to produce moderate after-tax returns to Growers, based on the achievement of the key performance variables as shown in Table 11.1.

Option 2 Returns

The scenario modelling shows that the financial returns vary between 7.6% and 9.9%. The IRR based on mid case assumptions is 9.1% and occurs at the mid point of the Lonsec benchmark range for medium term sawlog projects

The Project is expected to produce moderate after-tax returns to Growers, based on the achievement of the key performance variables as listed in as shown in Table 11.1.

Option 3 Returns

The scenario modelling shows that the financial returns vary between 7.2% and 8.4%. The IRR based on mid case assumptions is 8.0% and occurs at the low end of the Lonsec benchmark range for medium term sawlog projects. Lonsec would prefer to see higher return to Growers to compensate for the longer term of this project and the additional risk.

The Project is expected to produce low to moderate after-tax returns to Growers, based on the achievement of the key performance variables as listed in as shown in Table 11.1.

Option 4 Returns

The scenario modelling shows that the financial returns vary between 7.8% and 9.3%. The IRR based on mid case assumptions is 8.8% and occurs at the mid point of the Lonsec benchmark range for comparable projects.

The Project is expected to produce moderate after-tax returns to Growers, based on the achievement of the key performance variables as listed in as shown in Table 11.1. The combination of the floor price mechanisms in Options 1 and 2, together with the discounted Establishment Fee for Option 4, generate very robust returns from Option 4.

13.3. Impact of Gearing

The use of financing to effectively defer the payment of the Establishment Fee may facilitate a Grower's entry into the Project returns and also has the effect of increasing the after tax IRR for the Grower.

However, the Grower still has the obligation to repay the debt principal over the agreed term, plus the additional obligation to pay interest on the debt principal over the agreed term. Growers will need to assess whether these additional obligations increase the overall level of risk of participation in this Project, and whether the enhanced returns adequately compensate for any increase in the level of risk.

The geared returns in Table 13.2 are based upon the use of Grower finance, and compulsory insurance for the term of the loan, as offered by FEA Limited, using a minimum gearing rate 90%. Refer to the section 15 of the PDS and Table 15.1 for additional details about the finance packages.

Table 13.2 Scenario Modelling – Impact of financing on the mid case scenario after tax IRR

	Not geared	Gearing level	1 yr (P only)	3 yrs (P&I)	5 yrs (P&I)	7 yrs (P&I)	10 yrs (P&I)	12 yrs (P&I)	15 yrs (P&I)
Option 1	8.5%	100%	9.9%	13.2%	21.4% (1)	23.1% (2)	(3)	##	###
		50%	#	9.8%	10.9%	12.2%	(3)	##	###
Option 2	9.1%	100%	10.1%	12.0%	15.9%	20.4% (4)	22.4% (5)	22.9%(6)	###
		50%	#	10.1%	10.8%	11.6%	12.8%	13.7%	###
Option 3	8.0%	100%	9.6%	10.9%	13.5%	17.3% (7)	18.6% (8)	##	20.4% (9)
		50%	#	9.6%	10.7%	11.6%	12.3%	##	13.4%
Option 4	8.8%	100%	10.2%	10.8%	12.6%	16.0% (10)	16.6% (11)	16.7% (12)	17.2% (13)
		50%	#	9.5%	9.9%	10.2%	10.7%	11.0%	11.5%

The 1 Year principal only, interest free loan is offered only with 100% gearing.

This loan term is not offered for Options 1 and 3.

This loan term is not offered for Options 1 and 2.

(1) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 21.4% for a 5-year loan at 89% gearing
(2) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 23.1% for a 7-year loan at 73% gearing
(3) Due to the cash flow structure and limitations in IRR calculation, the IRR cannot be calculated
(4) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 20.4% for a 7-year loan at 87% gearing
(5) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 22.4% for a 10-year loan at 73% gearing
(6) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 22.9% for a 12-year loan at 67% gearing
(7) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 17.3% for a 7-year loan at 98% gearing
(8) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 18.6% for a 10-year loan at 73% gearing
(9) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 20.4% for a 15-year loan at 61% gearing
(10) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 16.0% for a 7-year loan at 95% gearing
(11) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 16.6% for a 10-year loan at 79% gearing
(12) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 16.7% for a 12-year loan at 73% gearing
(13) Due to the cash flow structure and limitations in IRR calculation, the highest measurable IRR is 17.2% for a 15-year loan at 67% gearing

13.4. Sensitivity Analysis

As stated the key financial performance measure that Lonsec focus on is the ungeared after tax IRR (Internal Rate of Return).

Chart 13.1 and 13.2 below provide further analysis across a nominal range where each parameter was varied over a nominal range of +/- 30%. In both relative and nominal terms, Option 1 and Option 2 and Option 3 returns show a moderate level of sensitivity. This is a result of the deferred fee structure.

Growers in Option 1 are not exposed to any direct costs throughout the Project, so therefore cost inflation has no impact on the IRR.

The Floor Price protection in Option 1 causes a flattening-out in the price sensitivity after prices have fallen by 20%.

In Option 2, the pruning fees are exposed to cost inflation, however the impact is minimal as shown in Chart 13.2. The Floor Price protection in Option 2 causes a flattening-out in the price sensitivity, but only after prices have fallen by 70%.

Chart 13.1 Sensitivity Chart of Option 1 IRR outcomes over a range of key parameters

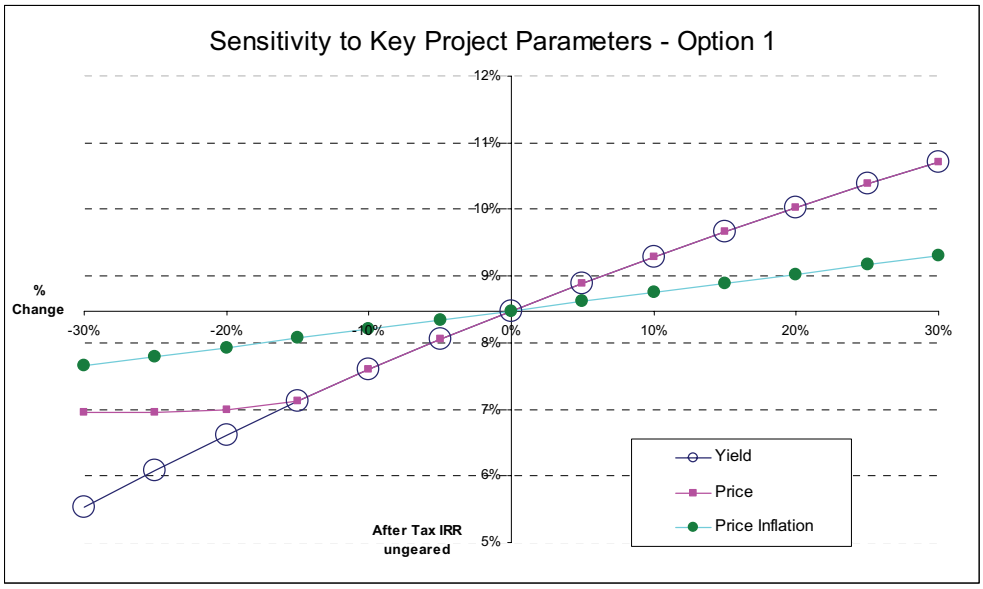


Chart 13.2 Sensitivity Chart of Option 2 IRR outcomes over a range of key parameters

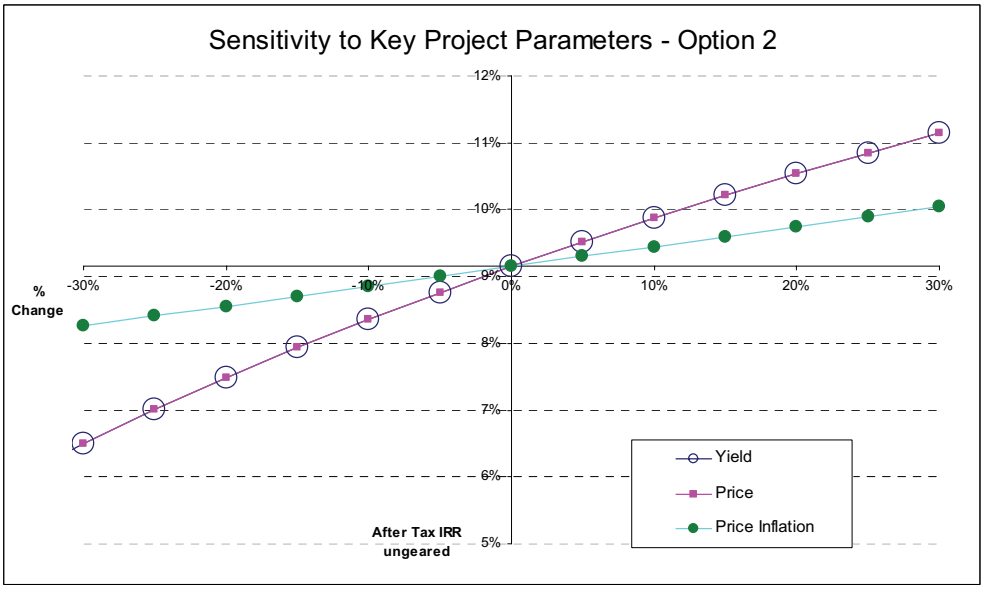


Chart 13.3 Sensitivity Chart of Option 3 IRR outcomes over a range of key parameters

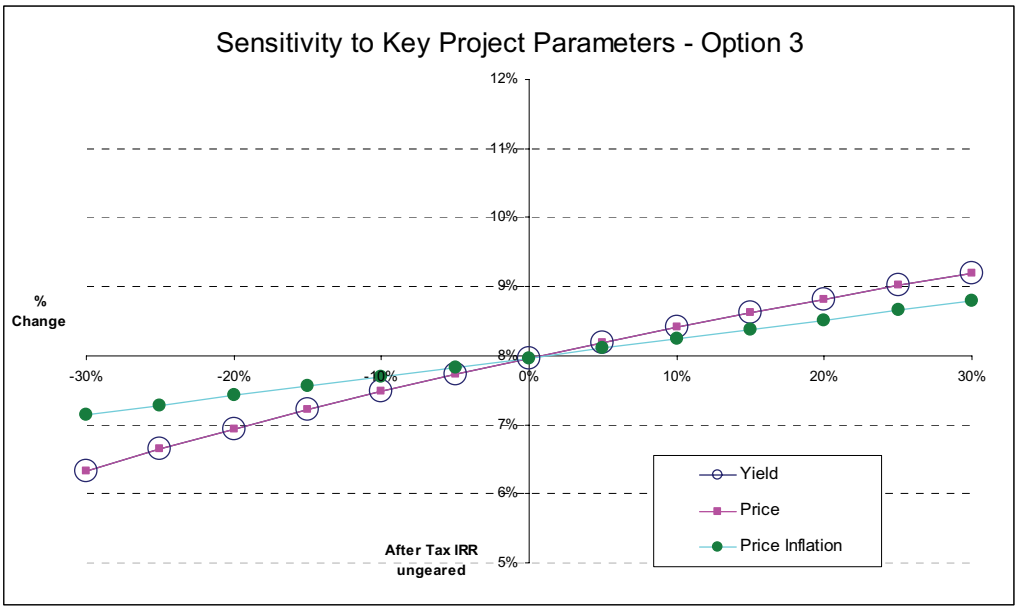
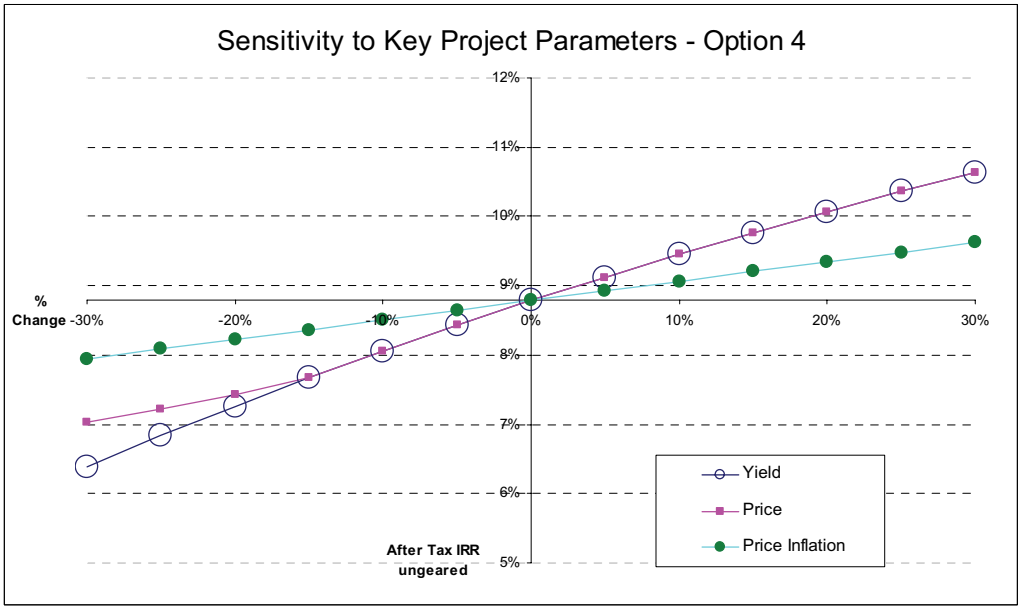


Chart 13.4 Sensitivity Chart of Option 4 IRR outcomes over a range of key parameters



13.5. Zero IRR Conditions

The following table shows the extent of the variations in yield and/or price that are needed to drive the after tax IRR to Growers down to zero.

At the zero after tax IRR position a Grower would receive back a sum of money exactly equal to the total of the initial outlay plus any annual payments that had been made. In this situation the Grower has not lost money, as such, but the Grower's financial position has been weakened because of the opportunity cost of that money, being the income foregone had the money been in a profitable investment.

The zero IRR position must not be seen as some form of a capital guarantee, because the Project Manager makes no such guarantee. If, for example, the price in Option 1 fell by 65% the after tax IRR would be negative 1.2% and the Grower would receive in total a sum of money less than the total of the initial outlay plus any annual payments that have been made.

Table 13.3 Mid Case Zero IRR conditions – Options 1 and 2

Option	Scenario	Pulpwood Stumpage ($/m^3)		Sawlog Stumpage ($/m^3)		MAI (m^3/ha/yr)	After Tax IRR
		Thinning	Harvest	Thinning	Harvest		
1	Price floor operative after 15% fall, not possible to achieve zero IRR	**$12.45**	**$14.11**		**$17.64**	27.0	**7.1%**
	Yield falls by 65%	$38.00	$41.00	$47.00	$51.00	**12.6**	**0.0%**
	Price & Yield fall by 41%	**$19.50**	**$22.10**		**$27.63**	**18.2**	**0.0%**
2	Price floor operative after 23% fall, not possible to achieve zero IRR	**$9.30**	**$10.54**		**$21.08**	27.0	**7.2%**
	Yield falls by 72%	$38.00	$41.00	$47.00	$81.00	**10.6**	**0.0%**
	Price & Yield fall by 48%	**$17.40**	**$19.72**		**$39.44**	**16.2**	**0.0%**

Table 13.4 Mid Case Zero IRR conditions – Options 3 and 4

Option	Scenario	Stumpage ($/$m^3$)					MAI m^3/ha/yr	After Tax IRR
		Pulpwood	Small sawlog	Medium sawlog	Large sawlog	Extra Large sawlog		
3	Price falls by 84%	**$1.80**	**$4.70**	**$7.70**	**$11.00**	**$12.90**	22.0	**0.0%**
	Yield falls by 84%	$11.00	$29.40	$48.20	$68.60	$80.30	**3.50**	**0.0%**
	Price & Yield fall by 60%	**$4.40**	**$11.80**	**$19.30**	**$27.40**	**32.10**	**8.80**	**0.0%**
4	Option 4 has a discounted Establishment Fee. Because of this, the Option 4 IRR cannot sensibly be driven down to zero. When Options 1, 2 and 3 all generate a zero IRR, Option 4 generates a 4.8% IRR.							

The numbers in **bold** type in Tables 13.3 and 13.4 indicate the assumptions that are being varied in the zero IRR analysis.

Consistent with the results in Table 13.1, the zero IRR analysis shows that both Option 1 and Option 2 have a low to moderate level of sensitivity resulting primarily from the deferred fee structure and the Floor Price mechanism. Option 3 has a low to moderate level of sensitivity resulting primarily from the deferred fee structure. Option 4 generates very robust returns because of the discounted Establishment Fee.

14. Taxation

14.1. Product Rulings

The Australian Taxation Office (ATO) has issued ATO Product Rulings PR 2008/31, PR 2008/32, PR 2008/33 and PR 2008/34 in respect of the FEA Plantations Project 2008. The Product Rulings generally confirm that a Grower in the Project is accepted to be carrying on a business of growing and harvesting wood for sale.

The Product Rulings also specify the tax deductions that will be allowed in respect of the following Project expenses:

- Establishment Fee
- Interest payable to FEA
- Insurance premiums

Access to the Product Ruling will be available from FEA Plantations free of charge or it can be downloaded from the ATO website at www.ato.gov.au

Growers should be aware that the Rulings:

- Will only apply to applications made after the Product Ruling has been issued.
- Will only apply to Growers who have their applications accepted on, or before, 30 June 2008.
- Will only be a ruling on the application of taxation law (as it stands at the date of issue).
- Will only be binding on the Commissioner of Taxation if the Project is implemented in the specific manner provided in the Product Ruling.

- Only addresses fees expected to be payable by Growers in the years ending 30 June 2008 to 30 June 2010. Fees incurred in future years are not covered by the Rulings, but it is presumed that these will also be deductible.

The ATO does not expressly or impliedly guarantee or endorse the commercial viability of the Project, the soundness or otherwise of the Project as an investment or the reasonableness or commerciality of fees charged in connection with the Project.

Prospective Growers in the FEA Plantations Project 2008 should, in all cases, seek their own taxation advice before investing in the Project.

14.2. History of compliance with previous Product Rulings

As at the date of this report, FEA Plantations has complied with all of the requirements of the Product Rulings relating to all of the projects for which it has acted as RE.

15. Other Grower Benefits

15.1. Grower Finance

Growers are offered up to 100% finance (including the GST component) from FEA, to facilitate investment in the FEA Plantations Project 2008. The loan will be secured by a fixed charge over the Grower's interest in the Woodlot. No application fees are payable. Growers must take out full replacement cost insurance if they borrow from FEA. The packages available are shown in the following table.

Table 15.1 Finance packages

Package	Interest Rate	Min. Deposit (inc. GST)	Repayment Terms
1 year	0%	0%	Monthly principal only
3 years	8.50%	0% to 10%	Monthly P&I
5 years	9.00%	0% to 10%	Monthly P&I
7 years	9.50%	0% to 10%	Monthly P&I
10 years	10.00%	0% to 10%	Monthly P&I
12 years#	10.50%	0% to 10%	Monthly P&I
15 years#	11.00%	0% to 10%	Monthly P&I

The common features contained in each of these loans are as follows:

- The Grower's application to participate in the Project has been accepted by FEA Plantations subject to finance approval.
- The Nominated Financier will take a fixed charge over the Grower's Woodlot(s).
- An initial deposit of between 0% and 10% of the Establishment Fee applies. P & I loans below $100,000 are available on a zero deposit. P & I loans of $100,000 or more require a 10% deposit. All one year interest free loans are available on a zero deposit.
- Interest rates will be fixed for the term of the loan.
- A default interest rate of 15% per annum will apply to all overdue and payable amounts.
- Growers who enter into these finance arrangements will be required to make equal monthly repayments of the outstanding balance.

Growers intending to make use of the finance facilities offered by third parties must be aware that there are material associated risks. In very broad terms these risks are:

- The financial situation of the Grower may change over time.
- The financial situation of the financier(s) may change over time.

15.2. Reports and Inspections

Growers will receive annual reports on the plantations prepared by FEA Plantations. In addition, the Independent Forester for the Project will report annually on the extent to which FEA Plantations is conducting the Project in a proper and efficient manner.

Growers are able to visit the plantations that comprise the Project by prior arrangement with FEA Plantations. The cost of travel to the plantations will be at the expense of the Grower.

15.3. Carbon Credits

In the event that any commercial carbon trades are negotiated, the after-cost benefit of these will be shared 50:50 between the Grower and the Responsible Entity.

16. Analyst Disclosure & Certification

Analyst remuneration is not linked to the rating outcome. The Analyst(s) may hold the product(s) referred to in this document, but Lonsec considers such holdings not to be sufficiently material to compromise the rating or advice. Analyst(s) holdings may change during the life of this document. The Analyst(s) certify that the views expressed in this document accurately reflect their personal, professional opinion about the financial product(s) to which this document refers.

Date Prepared: 29 April 2008
Analyst: Don Begbie
Release Authorised by: Jim Blackburn

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Product Rulings: At the time of conducting this research report, ATO Product Rulings had been granted to FEA Plantations Limited. Lonsec has not engaged a taxation specialist to provide advice on the implications of the Product Rulings, and proposed deductibility of the offer expenses to Growers. Taxpayers who are considering participating in the Project are advised to confirm with their taxation advisors that changes in the law have not affected the Project's Product Rulings since they were issued. The Product Rulings state that if the proposed arrangement is materially different from the arrangement that is actually carried out, the Rulings have no binding effect and will subsequently be withdrawn or modified.