



# Gunns Plantations Woodlot Project 2009

INDEPENDENT ASSESSMENT

This report has been prepared for financial advisers only

### Scope

Adviser Edge independent assessments are conducted by Barik Pty Ltd trading as Adviser Edge Investment Research (Adviser Edge) which has developed a key industry sector review process that follows a methodology developed specifically for this asset class.

### Key Principles

The underlying principles of the assessment process are to:

- identify the long term commercial potential of the project;
- evaluate project management’s capabilities, previous performance in the specific industry and the stability of the organisation;
- evaluate identified markets (domestic and international –existence, stability and growth potential);
- benchmark key performance assumptions and variables against industry and other MIS projects;
- weigh up the relevant risks of the project against projected returns;
- assess project structure and ownership;
- compare and substantiate project fees and expenses;
- determine if the project is structured in such a way as to protect investor’s interests; and
- allow an opinion to be formed regarding the investment quality of the project.

### Site Assessment

Adviser Edge conducts a detailed site inspection of the project, meets with all levels of project management and inspects the project’s infrastructure and market accessibility.

The site assessment considers the following areas:

- suitability of the project site for the purpose intended;
- performance of previous project stages located within close proximity to the proposed site;
- management skills, qualifications, capabilities and experience; and
- associated project risks and their management.

### Star Rating

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### Report Date

14 April 2009.

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## Investment Summary

Gunns Plantations Woodlot Project 2009 (the Project) provides investors with an opportunity to invest in the hardwood and/or softwood plantation industries. While the PDS provides information on four options, only offers for Option 1, Option 3 and the Blended Option are made under the PDS. These Options are as follows:

- The Option 1 investment (Option 1) is a 13-year rotation eucalypt hardwood plantation for the production of pulpwood
- The Option 3 investment (Option 3) is a 25-year rotation radiata pine softwood plantation for the production of sawlog and pulpwood
- The Blended Option investment (Blended Option) is a composite of Option 1 and Option 3, plus the inclusion of an Option 2 investment, which is a 20 year pruned sawlog option for the production of veneer logs and pulp logs. Option 2 is only available as part of the Blended Option, and is not available as a standalone investment

Gunns Plantations Limited (Gunns Plantations) will act as the Responsible Entity (RE) for this offer. Gunns Plantations was established in 1999. Gunns Plantations has been offering MIS plantation investments since 2000, and as at 30 June 2008 had raised approximately \$575 million in MIS projects in the forestry and horticultural industries.

Gunns Plantations is a subsidiary to Gunns Limited (Gunns), which will be responsible for the operational management of the Project. Gunns has a long history in the forestry industry, as the company was founded in 1875 and incorporated in 1951. The company is now Australia's largest hardwood producer, with extensive investment in downstream infrastructure. Gunns continues to focus its business in Tasmania, where its core strength lies, and the sites intended for use in this Project are mainly located in this region. Gunns manages over 275,000ha of land with 200,000ha under plantations, of which approximately 141,000ha is located in Tasmania.

The Option 1 plantations, together with the Option 2 part of the Blended Option, will be established on suitable sites in Tasmania. Option 3 plantations will be established in Tasmania and the Southern Slopes region of New South Wales. The sites for the Project have already been selected, with a majority having been assessed by the independent forester. This reduces the risk associated with investing in the Project, which is reflected in the Project's narrow IRR range.

The size of each woodlot is approximately 1ha for both Option 1 and Option 3, and 4ha for the Blended Option. Investors are required to pay an Establishment Fee of \$6,800 plus GST per woodlot for Option 1 or Option 3, and \$25,840 plus GST per

unit of the Blended Option. No ongoing annual fees will be levied to investors, except for pruning fees in the Blended Option. However, investors may choose to insure their woodlots. All ongoing maintenance, rent and sales commission fees are deferred and deducted as a percentage of harvest proceeds (15% plus GST). Following harvest, the net harvest proceeds (less all deferred management and lease fees) for each woodlot option will be pooled and distributed to investors.

The potential investment returns of each woodlot option will be affected by a number of performance parameters. The returns are expected to be most sensitive to variations in plantation growth rates, as these will affect the total yield of the woodlots. Variations in growth rates will also affect the average price paid for the timber, due to the impact of log volume on recovery rates and harvesting costs. In assessing returns, Gunns Plantations has used relatively more conservative yield and price assumptions when compared to peers. Based on the analysis of the various parameters that contribute to investment returns, Adviser Edge has estimated an indicative pre-tax IRR range of between 5.47% and 9.61% p.a. for Option 1, 5.06% and 9.10% p.a. for Option 3, and 6.99% and 11.08% p.a. for the Blended Option.

Based on the Adviser Edge investment ratings model, the Options in the Gunns Plantations Woodlot Project 2009 have achieved the following investment ratings:

- Option 1: 4.25 stars
- Option 3: 4 stars
- Blended Option: 4.5 stars

**Option 1: Adviser Edge Rating ★★★★★☆**  
**Option 3: Adviser Edge Rating ★★★★★☆**  
**Blended Option: Adviser Edge Rating ★★★★★☆**

### Project Details

Project Name	Gunns Plantations Woodlot Project 2009 Option 1 (hardwood), Option 3 (softwood) Blended Option (hardwood and softwood)
Product	Hardwood and softwood logs for pulp and paper manufacture and sawlog for timber processing
Responsible Entity/ Project Manager	Gunns Plantations Limited
Parent Company/ Operations Manager	Gunns Limited

### Investment Details

Investment Term	Option 1: Approximately 14 years Option 3: Approximately 26 years Blended Option: Approximately 26 years
Investment Unit Size	1ha per woodlot for Options 1 and 3 4ha for the Blended Option
Application Fee	\$6,800 (excluding GST) per woodlot for Option 1 and Option 3 \$25,840 (excluding GST) for the Blended Option
Ongoing Fee Structure	Deferred rent and maintenance fees (no ongoing annual payments, except voluntary insurance and pruning fees for the Blended Option)
Minimum Investment	One woodlot
Close Date for FY2009	30 June 2009
Investor Finance	Available
ATO Product Ruling	PR 2008/66 and 2008/66A (Option 1) PR 2008/68 and 2008/68A (Option 3) PR 2008/69 and 2008/69A (Blended Option)

### Investor Returns

Potential investment returns (p.a.)	Option 1: 5.47%–9.61% (pre-tax) Option 3: 5.06%–9.10% (pre-tax) Blended Option: 6.69%–11.08% (pre-tax)
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### Key Points:

#### Strengths of Project

- Gunns has a long history in the forestry industry and is considered to be one of the most experienced plantation forestry management companies in Australia
- Sites managed by Gunns in the regions selected are supported by empirical data to support growth yields for both hardwood and softwood timbers, with many sites exceeding initial estimates
- Gunns is considered to be in a good financial position
- The fee structure for each Option appropriately apportions risk between Gunns Plantations and investors, with fees considered to be reasonably priced
- The Blended Option provides diversified exposure to both the hardwood and softwood markets for both pulp, veneer and sawlog products

#### Weaknesses of Project

- Gunns Plantations is both the RE for the Project and a subsidiary of the intended buyer for the timber produced. However, Gunns has put in place systems to minimise any conflict of interest risk
- Gunns Plantations has reduced its on-ground presence in the New South Wales Southern Slopes region, as it has reduced the amount of plantation development in the region

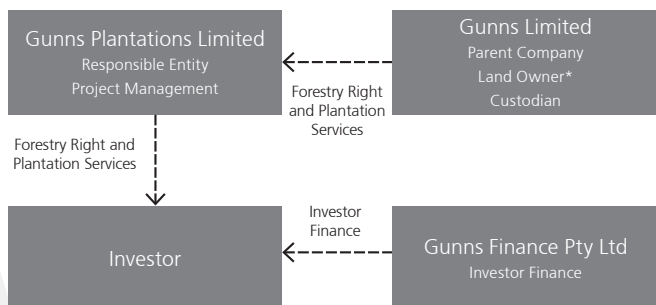
#### Other considerations

- A liquid secondary market does not currently exist for MIS forestry investments, although this may change in the future

#### Investor suitability

As a general note, investment in agribusiness should represent a balance between the various potential risks and the forecast returns. This Project offers a moderate to high-risk profile over the long-term, with reasonable pre-tax returns across the estimated range. This Project should be considered as part of a well-diversified portfolio.

### Key Counterparties



\* Landowner may also be other entities.

### Gunns Limited (Parent Company/Operations Manager)

Gunns was founded in 1875 and incorporated in 1951. It is Australia's largest hardwood producer and third largest softwood producer, currently operating eight timber sawmills, one veneer mill and five woodchip export facilities throughout Australia and New Zealand. Gunns' forestry operations are highly integrated and incorporate plantation establishment and management, woodchip, sawlog and veneer processing, retail hardware, and port handling. The company manages over 275,000ha of land with 200,000ha under plantation. In 2008, Gunns acquired softwood plantation company Auspine Limited, which owns and manages plantations in Tasmania and the Green Triangle region of South Australia and Victoria.

Gunns intends to establish a pulp mill facility at Bell Bay, Tasmania, which is subject to final environmental approval. Final funding also needs to be secured. The Federal Government has now approved 13 of the environmental modules, with the three remaining modules to be approved pending completion of hydrodynamic modelling of waste water discharge into Bass Strait. Gunns expects to announce a joint venture partner to assist in financing the pulp mill by April 2009.

Gunns has made the strategic decision to reduce new sales of MIS projects, as it has achieved its target objective of 200,000ha of plantations under management. However, further MIS activity is intended to maintain its plantation resource base going forward. MIS projects have contributed to over 100,000ha of Gunns' plantation resource base.

Gunns is listed on the Australian Securities Exchange (ASX Code: GNS), and as at 31 December 2008 had net assets of \$1.3 billion.

### Key Points:

- Gunns is a vertically integrated forestry company with substantial experience and a long history in the forestry industry
- Gunns and Gunns Plantations boast highly credentialed Boards of Directors
- Gunns has improved its financial position through an equity capital raise and the sale of the Auspine softwood resource
- Gunns is not reliant on MIS sales income for recurrent earnings
- There remains uncertainty in relation to the development of the Bell Bay pulp mill

### Board of Directors as at 2 April 2009

Board of Directors – Gunns Limited			
Director	Credentials	Industry	MIS
John Gay – Executive Chairman	★	★	★
Robin Gray – Non-Executive	★	★	★
Robin Holyman – Non-Executive	★	★	★
David McQuestin – Non-Executive	★	★	★
Christopher Newman – Non-Executive	★	★	★
Richard Millar – Non-Executive	★	★	★
David Simmons – Non-Executive	★	★	
Paul Teisseire – Non-Executive	★	★	

**Adviser Edge believes that Gunns' board members possess a sufficiently wide array of skills and capabilities necessary for the company to fulfil its role as operational manager of MIS projects.**

### Corporate governance and compliance

**Adviser Edge has reviewed corporate governance documents supplied by Gunns and believes that Gunns has adopted sound corporate and financial management procedures. Gunns has departed from the ASX Corporate Governance Council Principles of Good Corporate Governance and Best Practice Recommendations in relation to the appointment of Mr Gay as both the**

**Managing Director and Chairman.** *Gunns has indicated that Mr Gay will retire as Managing Director at the end of FY2009. Investors should also note that Gunns Plantations has departed from convention of appointing independent and external compliance committee members, and has instead adopted a sub-committee of the Gunns Plantations board to act as a compliance committee. This committee is composed of three independent and three executive members.*

### Financial performance

Key Financial Data					
Financial Profitability	Half year December 2008	Gunns Limited		Gunns Plantations Limited	
		Full year June 2008	Full year June 2007	Full year June 2008	Full year June 2007
Revenue (\$m)	427.64	861.95	682.21	124.64	144.84
Net profit (\$m)	33.57	64.48	76.42	37.06	53.52
Profit margin (%)	7.9%	7.5%	11.2%	29.7%	36.9%
ROCE (%)	n/a	7.2%	8.6%	54.3%	130.9%
ROE (%)	n/a	6.5%	8.6%	40.4%	98.0%
Market Measures					
EPS (basic/cents)	6.2	14.2	19.6	18.5	26.8
P/E ratio	n/a	16.8	16.7	n/a	n/a
DPS (cents)	2.0	10	14	0.00	2,500
Dividend yield (%)	n/a	4.2%	4.3%	n/a	n/a
Dividend payout ratio	32%	70%	71%	0%	9,343%
Financial Liquidity/Solvency					
Net working Capital (\$m)	-37.3	-190.0	111.9	86.6	50.3
Current Ratio	0.91	0.67	1.56	2.80	2.06
Quick Ratio	1.18	0.33	0.83	2.80	2.06
Debt to equity ratio	0.96	1.61	1.03	0.52	0.87
Gearing <sup>1</sup>	49%	62%	51%	34%	46%
Interest Coverage Ratio	2.60	2.40	4.00	3.61	9.14
NTA per Share	1.82	2.01	2.01	67.33	48.83

Source: Gunns Ltd and Gunns Plantations Ltd, Annual Report 2008 and Half Year Report 2008.

The financial ratios are based on share price information provided at the close of trading on the last day of the financial year for which they are quoted.

<sup>1</sup> Gearing is calculated as Total Liabilities/Total Assets.

Gunns has achieved a solid result in FY2008, with revenue growth of 26% to \$862 million. However, profit and earnings per share declined 15.6% and 27.5% respectively, to \$64.5 million and 14.2 cents per share. This result is attributable to the inclusion of the Auspine business into the company's results, as well as higher financing costs and higher non-operating costs. These mainly relate to the pulp mill project. Earnings per share increased substantially in the half year ending 31 December 2008, from 3.4 cents/share to 6.2 cents/share, mainly through

inclusion of the Auspine business for a full six-month period. However, after taking into account the share issue costs of the August 2008 non-renounceable rights issue, earnings per share declined slightly to 2.9 cents/share.

In 2008, Gunns took steps to stabilise its financial position. It has substantially improved its net working capital, through receipt of \$334.3 million in the aforementioned non-renounceable rights issue, and the divestment of approximately

75% of the Auspine softwood plantation resource for \$173.2 million at book value. These initiatives have improved Gunns' financial position substantially, with senior debt reduced from \$790 million to \$400 million. As at 31 December 2008, financial leverage reduced to 38% (from 52% at 30 June 2008), and the current ratio improved to 0.91 times (from 0.67 times at 30 June 2008). Had the Auspine transaction occurred prior to 31 December 2008, financial leverage would have been 32% and a current ratio of 1.5 times.

Gunns also has a policy of impairing the value of land as a result of the lease to investors in its MIS projects. This ensures that Gunns' balance sheet recognises the impact of investors' rights to land on the realisable value of Gunns' real property.

The Bell Bay pulp mill continues to be material to Gunns' financial position. Total expenditure on the pulp mill to 31 December 2008 was \$125.5 million. Should the pulp mill not go ahead, then it is expected that net assets for Gunns will reduce by up to 9% through the impairment of the capitalised costs of the development. Currently, the Bell Bay mill is expected to have a negligible impact on the balance sheet until final approval on the project is achieved, with costs of approximately \$200,000 per month.

**Adviser Edge believes that Gunns is in a solid financial position. Income is earned from a range of sources and Gunns is not reliant on MIS sales, which account for a small proportion of revenue. The capital management steps taken in 2008 have significantly improved the company's gearing levels, and its conservative MIS capital raising policy stands the company in good stead for future expenditure obligations.**

### Gunns Plantations Ltd (Responsible Entity/ Project Manager)

Gunns Plantations is the Responsible Entity (AFSL number 238701), for the Gunns Plantations Woodlot Project 2009. Gunns Plantations has raised approximately \$575 million in MIS projects in the forestry and horticultural industries. Under the **Management Agreement**, each investor will engage Gunns Plantations to provide the plantation establishment, management, harvesting and marketing services over the Project term. As Responsible Entity, Gunns Plantations delegates all operational management to Gunns Ltd under the **Establishment Services Sub-contracting Agreement** and **Maintenance and Pruning Services Sub-contracting Agreement**. Gunns Plantations has a separate Board of Directors, which is considered appropriate given the relationship of Gunns to the Project.

As part of its review, Adviser Edge has also reviewed the financial position of Gunns Plantations. Gunns Plantations is in a solid financial position, with interest cover at 3.6 times and minimal financial leverage through a loan from the parent company. While its future obligations to provide providing access to land and management services for investors are substantial (\$131.9 million in total, not increased for inflation), \$77 million of these obligations are not expected to accrue for at least another five years. Although difficult to analyse, this suggests that Gunns Plantations has sufficient financial resources to fulfil its obligations to investors.

#### Board of Directors – Gunns Plantations Limited

Director	Credentials	Industry	MIS
John Gay – Chairman	★	★	★
Robin Gray – Executive Director	★	★	★
Leslie Baker – Executive Director	★	★	★
Rodney Loone – Non-Executive Director	★	★	★
Patrick Sullivan – Non-Executive Director	★	★	★
Robert Graham – Non-Executive Director	★	★	

**Adviser Edge is confident that Gunns has the expertise and financial resources to meet its obligations to investors in the Project. However, It should be noted that a substantial amount of Gunns Plantations' asset backing consists of receivables from Gunns, which means that it is reliant on the continued financial health of the parent company. Adviser Edge believes that the composition of the Gunns Plantations board is prudent, with an appropriate level of independence and separation from the parent company.**

### Gunns Ltd (Operational Management)

Under the **Establishment Services Sub-Contracting Agreement** and **Maintenance and Pruning Services Sub-contracting Agreement**, Gunns is responsible for the operational management of the Project, including site preparation, planting and replanting, weed management, fertilising, and other silvicultural and management applications. Gunns also sub-contracts establishment and maintenance activities to third party contractors, with Gunns providing supervisory, management and logistics oversight. Gunns uses a range of third party contractors for the provision of all required activities.

#### Key Operational Personnel

Key Personnel	Credentials	Industry	MIS
Ian Blanden – General Manager	★	★	★
Robin Dickson – Operations Manager	★	★	★
Brent Donaldson – Operations Manager – Plantation Division	★	★	★



Key Operational Personnel			
Key Personnel	Credentials	Industry	MIS
Ian Ravenwood – Manager – North-west*	★	★	★
Harry Cusick – South-east Plantation Manager	★	★	★
Nicholas Mainwaring – Manager – North-east & Manager – Tamar Tree Farms	★	★	★
Chris Dare – Manager – New South Wales*	★	★	★

\* Chris Dare will replace Ian Ravenwood as Manager – North-west in May 2009. Ian Ravenwood will remain in the region to mentor Chris and to assist in the transition prior to retiring in 2011.

***Adviser Edge considers Gunns to be industry leaders in plantation establishment and management, and expects the Project plantations to be managed at a high standard. In addition, Gunns is considered to have sufficient operational capacity to manage the establishment of its plantations.***

***Gunns has incrementally expanded into the Southern Slopes region of New South Wales, which Adviser Edge believes to be an appropriate strategy to employ when expanding into a new region. While the size of the estate in New South Wales is not significantly large enough to justify a full-time manager, from an investment perspective Adviser Edge would have preferred an on-ground manager in the region. Nonetheless, the management systems that Gunns' has instigated for the region are considered reasonable.***

Additional analysis of the management counterparties can be found in Adviser Edge's Supplementary Document for the Gunns Plantations Woodlot Project 2009, available on the Adviser Edge website at [www.adviseredge.com.au](http://www.adviseredge.com.au).

### Investment Specifications

Maximum subscription	Option 1: 6,000 woodlots (6,000ha) Option 3: 3,000 woodlots (3,000ha) Blended Option: 500 units (2,000ha)
Locations	Option 1: Tasmania Option 3 and the Blended Option: Tasmania and Southern Slopes of New South Wales
Investment unit size	1ha per woodlot (Option 1 and 3) 4ha per unit (Blended Option)
Number of trees per unit	Option 1 and 2: 1,100 Option 3: 1,333
Minimum application	One woodlot
Liquidity	Illiquid – no established secondary market
Insurance	Not compulsory
Investor finance provider	Finance available through Gunns Finance Pty Ltd

## Project Structure and Agreements

When investors are accepted into the Project, they will be bound by a number of legal agreements that outline the rights and responsibilities of each party involved in the investment scheme. These agreements are outlined in the Project's Product Disclosure Statement (PDS). It is recommended that each potential investor and their adviser read and understand the Project agreements so as to ensure that the Project is suitable for the investor's needs.

### Option 1 – Hardwood woodchip regime (Option 1)

Option 1 involves the establishment of eucalypt hardwood trees for the production of woodchips for export pulp markets. Option 1 has an expected term of 13 years from the planting date, which must occur before 31 December 2010. Gunns will establish woodlots under Option 1 in Tasmania. Option 1 is expected to be commercially thinned when the trees reach nine years of age.

### Option 3 – Softwood sawlog and woodchip regime (Option 3)

Option 3 involves the establishment of radiata pine softwood trees for the production of sawlogs and woodchips for export and domestic markets. Option 3 has an expected term of 25 years from the planting date, which must occur before 31 December 2010. Gunns will establish woodlots under Option 3 in Tasmania (60%) and the Southern Slopes region of New South Wales (40%). Gunns intends to commercially thin Option 3 when the trees are approximately 13 and 18 years of age.

### Key Points:

- There are no ongoing fees & costs (except optional insurance and pruning fees for the Blended Option)
- Maintenance and rental fees are deferred and will be deducted from harvest proceeds
- Investors have the option to insure their woodlots

### Blended Option – Hardwood and softwood sawlog and woodchip regime

The Blended Option is comprised of two Option 1 woodlots, one Option 2 woodlot, and one Option 3 woodlot. The Option 2 woodlot component will be located in Tasmania, and involves the establishment of eucalypt hardwood trees for the production of woodchips for export pulp markets, and veneer logs for domestic and export markets. Option 2 has an expected term of 20 years from the planting date. Option 2 will be pruned on three occasions in the first ten years to develop clearwood suitable for veneer production, and will be commercially thinned when the trees reach nine years of age.

## Fee Schedule

The fees outlined in the following table relate to an investment made in the Project. The fee structure for the Project involves an Establishment Fee and deferred rental, maintenance and sales commission fees.

Initial and Deferred Fees (excluding GST)	
Payment Type	Cost Per woodlot (ex GST)
Establishment Fee	\$6,800 for Options 1 and 3 \$25,840 for the Blended Option
Deferred Maintenance Fee	5% of Wood Sale Proceeds <sup>^</sup>
Deferred Rental Fee	8% of Wood Sale Proceeds <sup>^</sup>
Sales Commission	2% of Wood Sale Proceeds <sup>^</sup>

<sup>^</sup> Wood Sale Proceeds are the proceeds derived from the sale of wood, which is expected to be sold on a stumpage basis.

The Establishment Fee is payable to cover land cultivation, seedling supply and planting. Maintenance and rental fees will be deferred and paid as a percentage of Wood Sale Proceeds (see above). All timber produced from the Project is expected to be sold on a 'stumpage basis', and proceeds will be distributed to investors after deferred fees and sales commission are deducted. Stumpage is the value that a purchaser pays to the investor for the timber as a standing crop. It excludes harvesting, transportation, processing and marketing costs for the end product, which are borne by the purchaser. There are no further costs and expenses charged under the Sub-Forestry Right Deed or the Management Agreement. Although the Constitution

provides that costs incurred by the Responsible Entity (RE) in performing its obligations under the Constitution and Project agreements may be deducted from harvest proceeds, the Constitution stipulates that most of the foreseeable expenses which may be incurred are the responsibility of the RE.

## Fee Analysis

With any forestry MIS project, the Establishment Fee is dictated by the actual development cost of establishing the plantation, including land preparation, seedling supply and planting costs, and other administration costs such as corporate overheads, marketing and PDS development expenses, and the profit margin taken by the Project manager.

Gunns Plantations has increased the Establishment Fee for Options 1 and 3 by 9.7%, from \$6,200 to \$6,800 per woodlot, excluding GST. The Establishment Fee for the Blended Option has increased by 4.2%, from \$24,800 to \$25,840 per woodlot, excluding GST. In addition to this, deferred fees have increased from 9% to 15% of net harvest proceeds for all Options, excluding GST. The changes in fee structure represent an overall increase in fees payable from the previous year's projects, as indicated in the following table.

Fee comparison with previous Gunns Plantations projects			
Project	Option 1	Option 3	Blended Option
2008 establishment fee	\$6,200	\$6,200	\$24,800
2009 establishment fee	\$6,800	\$6,800	\$25,840
2008 deferred fee <sup>^</sup>	9%	9%	9%
2009 deferred fee <sup>^</sup>	15%	15%	15%
NPV increase in fees <sup>*</sup>	15.61%	15.61%	7.23%

<sup>^</sup> Percentage of net harvest proceeds (calculated on the stumpage price).

<sup>\*</sup> The percentage increase of the net present value of overall fees from the 2008 Project (excluding GST), discounted at IRR of the investment.

**Despite the fee increase, Adviser Edge considers the fees charged by Gunns Plantations to be reasonably priced. The fee structure provides incentive for Gunns to seek positive outcomes for the Project. The Blended Option also offers a 5% discount on the establishment fee when compared to the individual options.**

Adviser Edge has analysed the Direct Forestry Expenditure (DFE) calculations provided to the ATO by Gunns Plantations as part of its Product Ruling application. Gunns Plantations has provided detailed information that calculates the breakdown of these costs, based on the expected site types intended for planting. Gunns Plantations has calculated the DFE excluding harvesting

costs. Adviser Edge considers this to give a better representation of the level of forestry expenditure.

## Risk apportionment

Risk apportionment refers to the level of risk that the Project Manager/RE shares with investors as a consequence of the Project fee structure. When ongoing Project fees are linked to harvest proceeds, and therefore Project performance, the risk sharing between investors and the Project manager is considered to be more evenly aligned. It also provides a measure of risk mitigation in the event of the RE's insolvency by providing the potential for adequate compensation for a replacement RE.

**Adviser Edge believes that the Project provides a reasonable level of risk apportionment. The deferred fee structure provides Gunns Plantations with an incentive to seek positive outcomes for the Project. As a result of the fee structure, the Project's sensitivity to changes in the underlying performance assumptions are reduced due to variation in deferred fees payable.**

## Additional Information

### Taxation advice

The Project has been issued with product rulings PR 2008/66 and PR2008/66A (Option 1), PR 2008/68 and 2008/68A (Option 3) and PR 2008/69 and 2008/69A (Blended Option). These provide certainty in relation to the taxation consequences of investing in the Project.

Adviser Edge does not conduct detailed analysis on the implications of the Project's Product Ruling, and it is advised that investors seek appropriate professional advice in relation to the full financial and taxation implications of their investment.

### Finance

Finance is available from Gunns Finance Pty Ltd to approved applicants. Basic loan details are provided below, and interested investors should contact Gunns for full loan terms and conditions, including associated fees and charges.

Finance options			
Financier	Term	Interest Rate	Repayment Option
Gunns Finance Pty Ltd	12 months	Interest Free	Monthly principal
	3 years	8.5%*	
	5 years	9%*	Nil deposit, monthly principal and interest (P&I)
	10 years	10%*	
	15 years <sup>^</sup>	10.5%*	

<sup>^</sup> Not available for Option 1.

\* Interest rates are fixed for the lesser of the term and five years.

Source: Gunns Plantations 2009.

## Plantation locations



Option 1, 3 and the Blended Option will be located in Tasmania. In addition, a proportion of Option 3 (approximately 40%) will be located in the Southern Slopes region of New South Wales. The majority of Gunns plantation estates are located in north-west and north-eastern Tasmania, with proximity to major towns of Hampshire, Deloraine and Launceston. In total, Gunns manages approximately 155,000ha in Tasmania. With the acquisition of Auspine, Gunns now also manages a significant plantation estate in the Green Triangle. Gunns also manages a relatively smaller plantation estate in the Tumut-Tumbarumba region (Southern Slopes) of New South Wales.

*The site visit to northern Tasmania demonstrated the extent of Gunns' vertical integration, from nursery through to processing, as well as its significant economies of scale and ability to secure high quality second rotation sites. The visit gave an insight into the experience and expertise of Gunns in establishing and managing plantations in the region.*

*The site visit to the New South Wales Southern Slopes region demonstrated Gunns' ability to establish and manage softwood plantations in that region. However, the visit also demonstrated the risks posed by low planting season rainfall. Gunns has implemented a number of strategies to minimise this risk in relation to the Project.*

*For a more detailed account of the site inspections performed by Adviser Edge, please refer to Adviser Edge's Supplementary Document for the Gunns Plantations Woodlot Project 2009.*

## Key Points:

- A stocking guarantee exists for two years after planting
- The site visit demonstrated Gunns' vertical integration and significant economies of scale
- Gunns has secured its land requirements for the 2009 Project, which reduces site selection risk and facilitates more timely establishment works

## Site selection

The Project sites have been selected in accordance with Gunns Plantation's site selection criteria. The independent expert describes the site selection criteria for all as regions as those which meet the following characteristics:

- Mild climate with uniform annual rainfall of 800mm to 1,500mm for eucalypt plantations and 650mm to 1,000mm for pine plantations
- Altitude of less than 600m above sea level for sites with westerly aspects, and an altitude of less than 700m above sea level for sites with an easterly aspect
- Fertile, well drained, gradational soils derived from granitic, basaltic or sedimentary bedrock
- Minimum soil depth of at least 600mm
- Land slope of no greater than 45%
- Net plantable area of no less than 20ha and in proximity to mills or ports

*Gunns has acquired the land required for the Project. The independent expert has inspected a majority of the land proposed for use and commented that the proposed harvest rotations and growth rates are feasible and likely. This provides Adviser Edge confidence that the Project is likely, on average, to achieve productivity objectives.*

## Species and varieties

Gunns Plantations proposes to plant two species for the Option 1 plantations: Tasmanian blue gum (*Eucalyptus globulus*) and shining gum (*Eucalyptus nitens*). For Option 3, Gunns Plantations proposes to plant radiata pine (*Pinus radiata*). These species are widely used as plantation species in Australia and have shown strong growth rates across a broad range of sites. All seedlings used for the Project will be sourced from genetically improved seed.

*The growth performance of Tasmanian blue gum, shining gum and radiata pine is well supported, with extensive yield data obtained over many years. The species are considered suitable for the Project's intended planting regions.*

**Site development and site maintenance**

Gunns will establish 1,100 stems per hectare (spha) for eucalypt species under Option 1 and 1,333 spha for investments under Option 3. Under the PDS, Gunns Plantations provides a minimum stocking guarantee of 90% of the original stocking rate for a period of two years after planting.

For a detailed analysis of site development and ongoing management operations, please refer to Adviser Edge's Supplementary Document on the Gunns Plantations Woodlot Project 2009, available at [www.adviseredge.com.au](http://www.adviseredge.com.au).

*Adviser Edge believes that Gunns has the means and resources to provide the necessary services under the Project agreements. Gunns has a long track record and is considered to be a leader in the forestry industry. The smaller size of Gunns' Southern Slopes estate, as well as Gunns' intention to limit establishment in this region, is likely to result in lower management resources when compared to Tasmania. Nonetheless, Adviser Edge believes that resources in this region are adequate for the Project.*

**Harvesting and processing**

For a detailed analysis of harvesting and processing, please refer to Adviser Edge's Supplementary Document on the Gunns Plantations Woodlot Project 2009.

*Gunns has well developed downstream infrastructure and systems capable of managing the Project from establishment to harvest and delivery, especially in Tasmania. In other regions, Gunns has employed a strategy of establishing plantations in well developed forestry regions that have extensive harvesting and processing industries.*

**Market Overview**

Product Type	Options 1 and 2	Option 3
Product type	Eucalypt hardwood timber	Softwood timber
Primary use	Veneer log and pulpwood	Sawlog and pulpwood
Key target market	Domestic, Japan, China and Korea	Domestic and Korea
Major competitors	Domestic and international pulpwood and sawlog producers	Domestic and international softwood producers

The long-term nature of the investment means that there is a degree of difficulty associated with forecasting market conditions over the Project term. Additional analysis of the various markets associated with the Project can be found in Adviser Edge's Supplementary Document on the Gunns Plantations Woodlot Project 2009, available on the Adviser Edge website at [www.adviseredge.com.au](http://www.adviseredge.com.au).

**Marketing strategy**

Gunns Plantations intends to sell the timber produced under the Project on a 'stumpage basis' as standing timber. The stumpage price is the price paid by the purchaser on the assumption that the purchaser will be responsible for the harvest, transport, processing and marketing of the timber.

It is intended that the hardwood and softwood pulpwood, sawlogs, and veneer logs produced in Tasmania will be sold to Gunns. Gunns has entered into an Wood Sale Agreement with Gunns Plantations for the timber produced on behalf of investors in the Project. Gunns Plantations is currently negotiating options for a purchaser of the softwood resource grown in the Southern Slopes region of New South Wales, with expressions of interest received from a number of third parties for its pulpwood and sawlog resource.

The woodchip resource is expected to be sold by Gunns into export markets, predominantly Japan, although there is potential for significant increase in sales to other Asian markets such as China, Indonesia and South Korea. Should it proceed, it is expected that the Tasmanian resource has the potential to be used in the Bell Bay pulp mill. Veneer logs are expected to be sold in domestic and export markets and the softwood resource is expected to be sold domestically to Gunns in Tasmania and local processors in New South Wales.

Gunns' Wood Fibre Division has significant experience as a purchaser and supplier of hardwood woodchips, with a history dating back to the late 1930s. Gunns has been exporting woodchip from Tasmania since the 1970s and currently operates

**Key Points:**

- Gunns is a vertically integrated forest products business and has extensive experience and significant investment in hardwood supply logistics
- The hardwood woodchip export market is expected to remain fairly stable over the long-term, and the markets for higher value hardwood and softwood sawlogs appear to be strong
- Gunns intends to enter into a Wood Sale Agreement that provides investors some downside price protection through a minimum price mechanism

six woodchip export facilities in Tasmania, located in Burnie, Tamar, and Triabunna, and one facility in Portland, Victoria.

***Adviser Edge considers Gunns to be industry leaders in the processing and marketing of woodchips and other forest products.***

***While Gunns is both the purchaser of the investors' timber resource and the parent of the Responsible Entity, Adviser Edge believes that Gunns Plantations has put adequate structures in place to ensure that the best interests of investors are considered, such as appointing a separate Board to Gunns Plantations.***

**Wood Sale Agreement**

Gunns Plantations intends to enter into a Wood Sale Agreement for the sale of the hardwood and softwood timber. This agreement requires Gunns to purchase all of the Project timber that is produced in Tasmania. This agreement requires that the purchase price must be a fair and reasonable price, which takes into account the proposed end-uses, prices paid by other parties in the region, industry practice, quality and timing, and other relevant information supplied by third parties.

As RE for the Project, Gunns Plantations may choose not to approve the purchase price and deliver to Gunns an alternative higher priced offer from a third party that is, otherwise on the same terms and conditions as the offer made by Gunns. Gunns will then have the option to match this offer. Should Gunns not match this offer, Gunns Plantations may sell the timber to the third party.

The Wood Sale Agreement also provides a minimum floor price that Gunns must pay for the timber, being no less than the average comparative price for the grade of timber. In addition, woodchips produced must also exceed a floor price, which is based on a proportion of the FOB price of Australian hardwood plantation woodchip at the time of the harvest.

*The minimum floor price and average comparative price mechanisms contained in the Wood Sale Agreement provide some downside protection for the wood produced as part of the Project, although a floor price for sawlogs produced under Option 3 would improve this agreement. Adviser Edge considers that this downside protection provides adequate compensation for the option received by Gunns (namely the first right of refusal). However, investors should note that the price protection provided under this agreement is subject to the long-term financial position of Gunns. Please refer to the Management section of this Report for more information on Gunns' financial position.*

The following section provides a discussion of the key project parameters that directly affect the performance of the investment. For a more detailed analysis of these parameters, please refer to Adviser Edge's Supplementary Document on the Gunns Woodlot Project 2009 available on the Adviser Edge website at [www.adviseredge.com.au](http://www.adviseredge.com.au).

## Timber Yield

Performance Parameters	Gunns Plantations Estimates		Gunns Plantations Estimates
	Option 1	Option 2 <sup>^</sup>	
Rotation Length	13 years	20 years	25 years
Average Mean Annual Increment (MAI)	24.7m <sup>3</sup> /ha/year	27.4m <sup>3</sup> /ha/year	21.8m <sup>3</sup> /ha/year
Timber Yield (per ha)	355m <sup>3</sup> *	547m <sup>3</sup>	550m <sup>3</sup> *

Source: Gunns Plantations, 2008.

<sup>^</sup> Contained in the Blended Option.

\* Includes yields generated from thinning harvests.

The average yield will depend on the quality of the land selected by Gunns Plantations, seasonal conditions over the growing period, and Gunns' management of the plantation. Significantly, Gunns Plantations has sourced all of its land requirements for the 2009 Project. This provides two significant benefits: greater certainty with respect to the productive capacity of the land, and the ability to undertake establishment works earlier and in a timely manner.

***The independent expert anticipates that the yields estimated by Gunns Plantations are achievable for the Project. While seasonal conditions and on-going Project management are important in achieving final outcomes, site selection also has an important bearing on total productivity. The independent expert has inspected the majority of the sites selected for the Project and considers these sites to have high productivity potential. This has increased Adviser Edge's confidence in the yield targets estimated by Gunns Plantations.***

### Past performance

While Gunns has a long history in the forest products industry, its experience in the MIS industry is not as long, with the first MIS project offered by Gunns Plantations in 2000. Gunns Plantations has provided growth data in relation to the 2000 and 2001 Projects. This growth data suggests that Options 1 and 2 of both the 2000 and 2001 projects are exceeding the growth rates forecast. Indeed, Gunns has commenced thinning operations for the 2001 project in April 2009. Thinning will also

## Key Points:

- Pricing data for hardwood and softwood pulpwood, sawlogs and veneer is reasonably supported
- Land has already been identified, providing greater confidence in yield targets, although they will continue to be dependent on ongoing management and seasonal conditions
- Gunns Plantations has a strong track record, with expectations for its 2000 and 2001 MIS projects considered to be significantly above initial forecasts. However, it should be noted that these projects represent a very small proportion of Gunns Plantations' MIS plantation estate.

be conducted on Option 1 plantations from this Project, although no thinning was originally planned.

It should be noted that these results are for a total of 1,693ha and are located entirely in Tasmania. Gunns has a MIS project plantation estate of approximately 100,000ha, of which 2,802ha of radiata pine is located in New South Wales. The remaining estate located in Tasmania. Gunns rapidly expanded its plantation estate in 2002, with MIS offerings exceeding 9,000ha in each subsequent financial year. Gunns has not provided inventory information on subsequent MIS projects. However, Gunns has provided Adviser Edge with all previous independent forester's report for each of its projects. These reports indicate that the 2002 to 2008 projects are progressing well and have been managed to a high standard. The reported dominant heights for the 2002 to 2008 projects suggest that while these projects may be on track, they do not appear to be exceeding the excellent growth performances of the 2000 and 2001 projects, although this is difficult to determine until inventory data has been collected.

***Gunns has a track record of excellent silvicultural management, and the past performance information provided represents one of the better track records in the forestry MIS industry. While past performance is not necessarily a good indicator for future performance, Gunns' past performance, focus on established regions and access to good second rotation sites provides confidence that Gunns is capable of achieving its objectives.***

## Sawlog Recovery

Sawlog recovery is a function of genetics, site characteristics, and stand management. Sawlog recovery has a significant influence on price, and thereby the investment returns for each



investment option. The main factors that influence sawlog recovery include the straightness and size of the log, and the presence of other log defects including damage caused during transportation and processing. Sawn timber processors are prepared to pay higher prices for straighter logs, as they are able to achieve a higher recovery rate on these logs.

Recovery of sawlog (Option 3 – softwood)				
Operation	x < 24cm	24cm < x < 32cm	32cm < x < 45cm	x > 45cm
Thinning 1	33%	–	–	–
Thinning 2	20%	31%	11%	–
Clearfell	16%	29%	26%	19%

Source: Gunns, 2009.

Recovery of sawlog or veneer (Option 2 – hardwood)^	
Operation	Sawlog or veneer
Thinning 1	–
Clearfell	40%

^ Option 2 component of the Blended Option.  
Source: Gunns, 2009.

**The sawlog and veneer recovery information provided by Gunns Plantations is contained in the independent expert report. The figures adopted for the Project are in line with the figures proposed by peer projects for the thinning and final clear fell harvest operations, having regard to the species planted and term of the proposed rotation. The sawlog recovery estimates provided are considered to be within the ranges Adviser Edge considers achievable.**

### Pulpwood and Sawlog Price

The following price estimates were provided by Gunns Plantations, and are based on information incorporated in the independent forester’s reports. These values are given in present-day terms.

Price parameters (Option 1 and 2 – hardwood)		
Average stumpage price	Thinning	Clearfell
Pulpwood (\$/m³)	39.00	42.00
Veneer	n/a	\$136.00

Source: Gunns Plantations 2009.

Price parameters (Option 3 – softwood)	
Average stumpage price	Thinning (\$/m³) and Clearfell
Pulpwood	19.00
x < 24cm	29.40
24cm < x < 32cm	48.65
32cm < x < 45cm	69.30
x > 45cm	78.75

Source: Gunns Plantations, 2009.

Gunns proposes that investors will be offered a stumpage price for the harvested timber. The stumpage price is determined from the free on board (FOB) or mill door prices, and converted back by subtracting all the costs of harvesting, chipping, transportation and marketing, and by incorporating any conversion factors (i.e. volume-to-weight, green-to-dry, etc.).

Investors in Options 1 have the benefit of a ‘floor price’ mechanism, which is outlined in detail in the Wood Sale Agreement. The floor price is a function of the prevailing FOB price and therefore acts as a protection mechanism for investors against future increases in the cost of harvesting, transporting and processing the timber.

### Hardwood

The independent forester has determined the stumpage price for pulpwood as being \$39/m³ at thinning and \$42/m³ at final harvest. Higher prices should be expected at final harvest as log sizes and densities are expected to be higher than at thinning. Pulpwood stumpage prices are affected by different factors depending on the species (i.e. pulping quality), distance to port, size of plantation and extraction method used.

The independent forester has determined that the stumpage price of \$136/m³ for clearwood veneer, which is grown as part of Option 2, is reasonable and achievable. This price is based on an analysis of prices for native eucalypt veneer logs and softwood veneer logs.

**Adviser Edge is satisfied with Gunns Plantations’ budget for current pulpwood and veneer log stumpage prices. Given the long-term nature of the Project, Adviser Edge considers applying a zero real price inflation assumption to be a prudent investment approach.**

### Softwood

The stumpage price for softwood logs ranges from \$19/m³ for pulpwood to \$78.75/m³ for >45cm softwood logs.

As stated previously in the Marketing section of this report, the price of all softwood grades has fallen in real terms over the last decade. While it is difficult to forecast future price trends, it is expected that the market outlook will strengthen if the

anticipated shortfall in the supply of softwood and hardwood sawlog occurs in key plantation regions. The demand for softwood resources, which is primarily driven by the rate of housing development, is the other primary factor that will dictate prices at harvest. Given the cyclical nature of the housing market, it is expected that the demand for softwood resources will fluctuate over the next 25 years.

***The stumpage prices for softwood have fallen in real terms in the past year. Adviser Edge considers the most recent market values to be the most appropriate when calculating the estimated IRR returns range. Gunns Plantations has assumed that stumpage prices will increase by 2.9% per annum, which is consistent with Gunns Plantations' inflation expectations.***

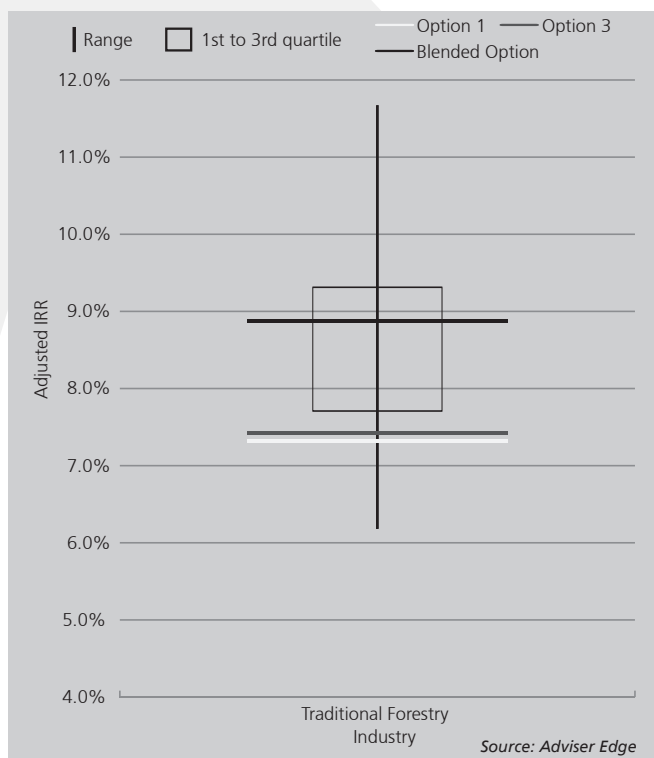
***For a more detailed analysis of the market for the products to be produced in the Project, please refer to the Gunns Woodlot Project 2009 Supplementary Document.***

The following section provides an analysis of the potential investment returns for the Project. Please note that this analysis is based on estimated performance assumptions, which may change over the Project term. Investors should be aware of the way in which these assumptions may influence their returns, and should seek additional professional advice to determine whether or not this investment is suitable for their own risk and return objectives.

<b>Adviser Edge potential IRR range (pre-tax)*</b>			
Gunns Plantations Woodlot Project 2009			
	Pre-Tax	Post-Tax**	Adjusted IRR
Option 1	5.47%–9.61%	5.47%–9.61%	7.33%
Option 3	5.06%–9.10%	5.06%–9.10%	7.42%
Blended Option	6.69%–11.08%	6.69%–11.08%	8.87%

\* The range is provided as a guide only and investors should seek additional professional advice regarding the impact of changes in key variables on Project returns given their individual financial circumstances. The analysis does not consider investor finance arrangements or insurance premiums.  
 \*\* The analysis assumes a 46.5% marginal tax rate, that investors are registered for GST, and that all GST is rebated in the year paid.

Using a standardised adjustment model, Adviser Edge has calculated indicative pre-tax adjusted IRR for each Option as shown in the table above. The following chart benchmarks these adjusted return estimates against other traditional forestry projects researched by Adviser Edge in FY2008.



When compared to all forestry MIS projects researched by Adviser Edge in FY2007-08, the adjusted IRR estimate lies

slightly below the first to third quartile for Options 1 and 3. The adjusted IRR for the Blended Option is slightly above the first to third quartile.

### Investment Analysis Performance Assumptions

The estimated Project returns provided by Adviser Edge have been calculated using various performance assumptions. The key assumptions adopted by Adviser Edge are presented in the following table. These assumptions have been determined from information provided in the PDS, directly by Gunns Plantations, from the independent foresters report, and from independent research performed by Adviser Edge. The following table also includes the performance assumptions adopted by Gunns Plantations, as discussed in the Performance Parameters section of this report.

Performance assumptions	Adviser Edge	Gunns Plantations/ Independent Forester
<b>Hardwood Yield (Option 1)</b>		
• Thinning	62m <sup>3</sup> /ha	62m <sup>3</sup> /ha
• Clearfell	260m <sup>3</sup> /ha	260m <sup>3</sup> /ha
<b>Hardwood Yield (Option 2)^</b>		
• Thinning	92.3m <sup>3</sup> /ha	92.3m <sup>3</sup> /ha
• Clearfell	454.8m <sup>3</sup> /ha	454.8m <sup>3</sup> /ha
<b>Softwood Yield (Option 3)</b>		
• First thinning	88m <sup>3</sup> /ha	98m <sup>3</sup> /ha
• Second thinning	108m <sup>3</sup> /ha	107.7m <sup>3</sup> /ha
• Clearfell	345m <sup>3</sup> /ha	344.6m <sup>3</sup> /ha
<b>Average hardwood stumpage price (Option 1)</b>		
• Thinning	\$39.00/m <sup>3</sup>	\$39.00/m <sup>3</sup>
• Clearfell	\$42.00/m <sup>3</sup>	\$42.00/m <sup>3</sup>
<b>Average hardwood stumpage price (Option 2)^</b>		
• Thinning	\$39.00/m <sup>3</sup>	\$39.00/m <sup>3</sup>
• Clearfell	\$75.20/m <sup>3</sup>	\$79.20/m <sup>3</sup>
<b>Average softwood stumpage price (Option 3)</b>		
• First thinning	\$15.44/m <sup>3</sup>	\$22.43/m <sup>3</sup>
• Second thinning	\$36.49/m <sup>3</sup>	\$35.80/m <sup>3</sup>
• Clearfell	\$50.39/m <sup>3</sup>	\$53.69/m <sup>3</sup>
Stumpage Price Inflation	2.9%	2.9%
Cost Inflation	2.9%	2.9%

^ Option 2 is a component of the Blended Option, and is not available as an individual investment option.

### Hardwood

Adviser Edge has adopted Gunns Plantations' yield estimates for eucalypt hardwood trees in Tasmania. Adviser Edge is confident of the productive potential of *Eucalyptus nitens* on sites in the Tasmanian region that meet Gunns Plantations' selection criteria.

***Adviser Edge is satisfied that Gunns Plantations has the skills and expertise to establish and manage eucalypt hardwood plantations in Tasmania. Gunns Plantations has developed a detailed site selection process to select suitable land, and Adviser Edge believes that yield estimates are achievable, provided that average rainfall is received over the growing period and the plantations are appropriately managed.***

Adviser Edge has adopted Gunns's estimates in relation to stumpage prices for eucalypt hardwood trees in the Tasmanian region. Gunns has committed to a Wood Sale Agreement to purchase the timber at harvest and thinnings, and to pay the prevailing stumpage price. This Wood Sale Agreement provides some downside protection through the inclusion of a minimum floor price that is equal to a fixed percentage of the FOB woodchip price for hardwood pulpwood and veneer logs. The FOB woodchip price is the price paid by the end purchaser of the woodchip delivered onto the ship at port. This provides investors with some protection against higher than expected harvesting and transportation costs. In addition, the Wood Sale Agreement ensures that the price received by investors for their woodchips is comparable to the price of Gunns' other hardwood purchases in the region.

Based on a 48% wood fibre content and a FOB price assumption of \$198.50 BDMT, the minimum price that must be paid under the Wood Purchase Agreement for hardwood pulpwood is contained in the following table. It should be noted that the most recently negotiated FOB price for plantation hardwood woodchip is \$207.40 BDMT which further improves the minimum price.

Price under the Wood Sale Agreement*	
Category	\$/green tonne
Pulpwood at thinning	\$33.44
Pulpwood at clearfall	\$37.16

\* Assumes 48% wood fibre content and \$198.50 BDMT woodchip price.

***Adviser Edge has reviewed Gunns Plantations' assumed prices and considers them to be achievable. There is also potential price upside through price premiums for deliveries of homogenous plantation woodchip and any unpruned sawlogs and veneer logs that are recoverable from the plantation.***

### Softwood

Gunns Plantations has budgeted an average MAI of 22m<sup>3</sup>/ha/year, which is within the achievable yields estimated by Adviser Edge for softwood in the regions provided. However, these yields will only be possible if high quality sites are selected, quality management protocols are adhered to, and average rainfall is experienced throughout the rotation. Adviser Edge has taken a slightly more conservative approach in assessing potential returns. Adviser Edge has adopted slightly lower yield estimates (21.6 MAI) for cash flow modelling purposes, recognising the risks associated with site selection and operational management when growing softwood.

***Gunns Plantations' assumptions in relation to yields are broadly in line with Adviser Edge's expectations for softwood plantations in the proposed regions.***

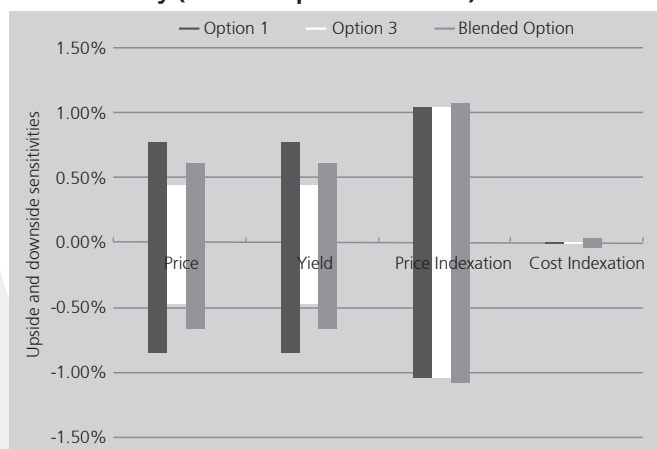
Adviser Edge has taken a slightly more conservative approach to softwood prices when compared with the industry expert. While the prices budgeted by the expert are considered achievable, Adviser Edge has used slightly lower price assumptions for the first thinning and the clearfall harvest. Despite using higher price assumptions for larger sawlogs, the weighted stumpage price used by Adviser Edge has been adjusted down slightly to reflect a degree of conservatism in relation to the prices achievable for the pulplogs and small to medium sawlogs.

***Gunns Plantations' price assumptions are broadly within Adviser Edge's range of potential prices. Adviser Edge has adopted higher price assumptions for the larger sawlogs but lower price assumptions for pulplogs and small to medium sawlogs. This is reflected in the average stumpage prices for earlier thinnings, which are expected to have a higher proportion of small to medium logs compared to the clearfall harvest.***

### Sensitivities

The table below illustrates the sensitivity of investment returns (IRR) given an isolated change in key modelling factors. For the purpose of this analysis, Adviser Edge has considered the sensitivity of returns to isolated changes in yield, and price and cost indexation parameters. Yield sensitivity reflects a movement of 10% around the Adviser Edge performance assumption, while price and cost index sensitivities reflect the impact of a 100 basis-point (1.0%) movement in the price and cost inflation rates estimated by Adviser Edge.

**IRR sensitivity (based on pre-tax returns)**

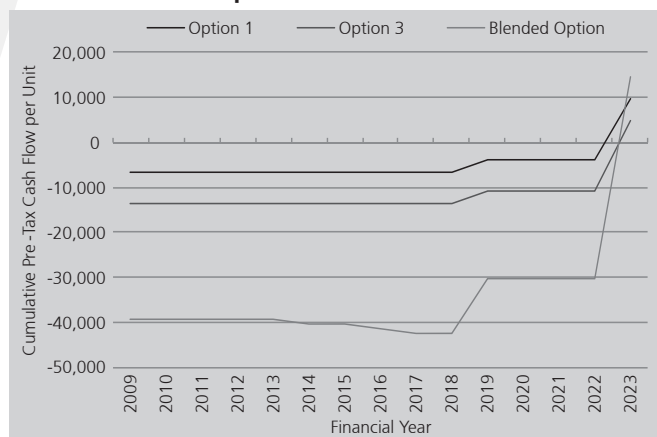


The analysis illustrates that the potential IRR of this investment is most sensitive to variations in price indexation. Option 3 has the lowest level of sensitivity, as it has the longest term. This reduces the impact of changes in price and yield assumptions on overall potential IRR. As it is assumed that for each Option the pulpwood and sawlogs will be sold on a stumpage basis, the variation in the rate of cost inflation has minimal impact on sensitivity. In reality, increased harvesting, haulage and processing costs will be reflected in lower stumpage prices.

**Pre-Tax Cash Flow per Unit**

The Gunns Plantations Woodlot Project 2009 provides investors an opportunity to invest in three different plantation regimes and species that provide cash flows over different time periods. An indicative cumulative pre-tax cash flow for each of the Options is presented in the following charts. These cash flows have been calculated using the performance assumptions adopted by Adviser Edge.

**Grower cumulative pre-tax cash flow**



**Post-Tax Potential**

The post-tax returns earned by an investor will depend on the investor’s marginal tax rate when harvest returns are received. The post-tax IRR range provided by Adviser Edge assumes that the investor maintains the same marginal tax rate of 46.5% throughout the investment term. However, it is likely that an investor’s tax status will change over the life of the Project. A change in tax status may result from a change in circumstance for the investor, or a change in tax policy administered by the Australian government. It is important that investors are aware of how these changes may affect the Project’s post-tax performance.

*Adviser Edge recommends that investors consult with qualified specialists who understand how changes to an investor’s tax status may impact investment returns.*

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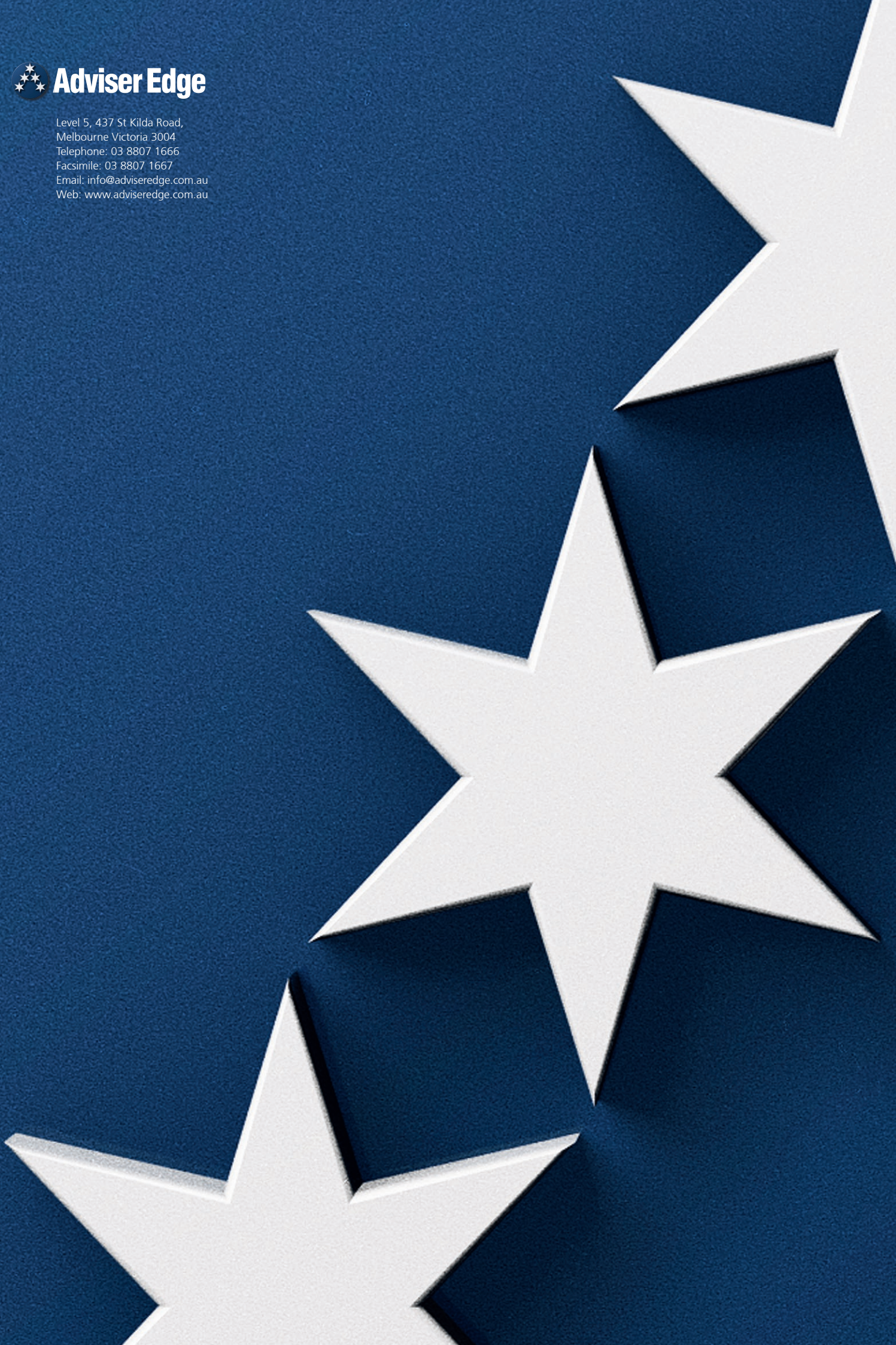
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# Gunns Plantations Woodlot Project 2009 – Supplement

INDEPENDENT ASSESSMENT

This report has been prepared for financial advisers only

### Scope

Adviser Edge independent assessments are conducted by Barik Pty Ltd trading as Adviser Edge Investment Research (Adviser Edge) which has developed a key industry sector review process that follows a methodology developed specifically for this asset class.

### Key Principles

The underlying principles of the assessment process are to:

- identify the long term commercial potential of the project;
- evaluate project management’s capabilities, previous performance in the specific industry and the stability of the organisation;
- evaluate identified markets (domestic and international –existence, stability and growth potential);
- benchmark key performance assumptions and variables against industry and other MIS projects;
- weigh up the relevant risks of the project against projected returns;
- assess project structure and ownership;
- compare and substantiate project fees and expenses;
- determine if the project is structured in such a way as to protect investor’s interests; and
- allow an opinion to be formed regarding the investment quality of the project.

### Site Assessment

Adviser Edge conducts a detailed site inspection of the project, meets with all levels of project management and inspects the project’s infrastructure and market accessibility.

The site assessment considers the following areas:

- suitability of the project site for the purpose intended;
- performance of previous project stages located within close proximity to the proposed site;
- management skills, qualifications, capabilities and experience; and
- associated project risks and their management.

### Star Rating

Projects are awarded a star rating out of a possible five stars and placed on the Adviser Edge web site [www.adviseredge.com.au](http://www.adviseredge.com.au)

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### Report Date

14 April 2009.

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### Gunns Limited (Parent Company)

Gunns Limited was founded in 1875 and incorporated in 1951 and is one of Australia's leading forestry companies. Gunns is the parent company of the responsible entity of the Project, Gunns Plantations Limited (Gunns Plantations) (AFSL number 238 701). Gunns is listed on the Australian Stock Exchange (ASX Code: GNS) and had net assets of \$1.3 billion as at 31 December 2008.

*In this Supplementary Document, Gunns refers to the parent company or any underlying subsidiary.*

Gunns has operations in plantation establishment, timber processing and logistics, which it undertakes on its own behalf, with joint venture partners and on behalf of investors in MIS projects. In addition to this, Gunns has businesses in hardware retailing, construction, horticulture MIS (winegrapes and walnuts) and owns Tamar Ridge Estates, which is a 400ha vineyard located in the Tamar Valley.

Gunns employs approximately 2,500 staff. Gunns also outsources harvesting and plantation establishment and maintenance activities to contractors, with Gunns staff providing supervisory, management and logistics functions.

Gunns has substantially expanded its operations on mainland Australia by acquiring Auspine Limited, which has significant softwood resources in the Green Triangle region and in Tasmania. Recently, Gunns has sold a majority of the Auspine softwood resource at book value, although Gunns continues to own the underlying freehold property and retains harvest rights to the timber. This land can be used by Gunns for second rotation plantations in the future.

Gunns is continuing with its intention to establish a pulp mill in Bell Bay, Tasmania, having received state and federal approval to build the mill. Significantly, environmental approval has also been conditionally obtained, subject to the results of further hydrodynamic modelling. It is expected that the mill will cost approximately \$1.7 billion and produce over 820,000 air dry tonnes of bleached kraft pulp each year. The Bell Bay mill was chosen due to its proximity to existing wood supply, and access to infrastructure including ports, water and gas.

### Corporate governance and compliance

The Risk Management Strategy has been developed to identify the risks associated with the Gunns business, and to manage these risks to reduce the occurrence and impact of any adverse events. The Code of Conduct has been developed to ensure that the officers and employees of Gunns conduct themselves in an honest and ethical manner.

In addition, Gunns Plantations has established a compliance committee to ensure that the Constitution and relevant Project

agreements are adhered to. The compliance committee is a sub-committee of the board of Gunns Plantations.

*Adviser Edge has reviewed Gunns' corporate governance and risk management procedures, and believes that they are sufficient to supervise the managers of the Project. Nonetheless, Adviser Edge would have preferred the compliance committee members be separate from the board of Gunns Plantations.*

### Capital raising history

MIS capital raising history – Gunns Plantations Ltd			
Project Type	Financial Year	Area (ha)	Capital Raised (\$ million)
Forestry	2000	453	2.15
Forestry	2001	1,240	5.95
Forestry	2002	15,013	59.3
Forestry	2003	13,017	52.0
Forestry	2004	9,162	39.0
Winegrape	2004	90	5.3
Forestry	2005	11,199	69.4
Wingrape	2005	41	3.2
Forestry	2006	10,500	65.1
Winegrape	2005	35	2.7
Forestry	2006	1,342	8.3
Walnuts	2006	69	2.3
Forestry	2007	21,206	131.5
Walnuts	2007	111	3.4
Winegrape	2007	50	3.9
Forestry	2008	16,972	105.2
Walnuts	2008	2,425	14.1
Winegrape	2008	150	2.4
<b>Total</b>			<b>\$575.2</b>

### Gunns Plantations Ltd (Responsible Entity/Project Manager)

*The following contains an overview of Gunns's key operational personnel, as outlined in the main report.*

Ian Blanden has been the General Manager of Gunns Plantations since 1999, having previously had 12 years experience with Tasmanian company North Forest Products in various management and forester roles. Ian holds qualifications in forestry from the Australian National University and Canterbury University, New Zealand. Ian is also a director of the Tasmanian Agricultural Productivity Group, is a Fellow of the

Australian Rural Leadership Foundation, and is a Member of the Institute of Foresters of Australia.

Robin Dickson has been the Operations Manager of Gunns Plantations since 1999. In this role, Robin is responsible for ensuring that all operational activities undertaken by Gunns meet the requirements of Gunns Plantations and the MIS projects. Prior to joining Gunns, Robin has had 14 years experience as Operations Manager for Forest Resources, Tasmania.

Brent Donaldson is the Operations Manager – Plantation Division. Brent has over 12 years prior experience in various management and forestry roles with ForestrySA, Forestry Tasmania, PF Olsen and Company, and the Forestry Corporation of New Zealand. Brent holds tertiary qualifications in forestry from the University of Canterbury.

Ian Ravenwood is the Forestry Manager for north-west Tasmania. Ian has over 23 years experience in the Tasmanian plantation industry, in addition to previous agronomic experience in horticulture and agriculture. Ian has managed Gunns Plantations' north-west plantations since 1999, and is responsible for Gunns' forestry seedling nursery operations in Somerset, Tasmania. Ian holds tertiary and postgraduate qualifications in Science, and has completed a Masters of Business Administration. Ian is intends to retire in 2011, with Chris Dare expected to assume responsibility in May 2009.

Chris Dare is the north-west Tasmania Regional Manager, having previously been responsible for Gunns Plantations' softwood plantation and walnut orchard in New South Wales. Chris has over 12 years of experience in the forestry industry, and has been responsible for overseeing the establishment of over 8,000ha of plantations annually and the maintenance of an estate of approximately 20,000ha.

Harry Cusick was appointed south-east Tasmania Plantation Manager in 2001, having over 27 years previous experience with North Forests, Rio Tinto, Associated Pulp and Paper Mills, and Tasmanian Pulp and Forest Holdings. Harry has had extensive training in forestry, agriculture and management.

Nicholas Mainwaring has been appointed Plantation Operations Manager for north-east Tasmania, having had previous forestry experience with North Forest Products as a Forest and Land Assessor. Nick holds qualifications in Forestry Management.

#### **Independent experts**

Gunns Plantations has engaged Gerry Cross of Van Diemen Forestry Consultants to provide an independent report on the proposed forestry management of the Project and on the potential markets for the timber produced.

#### **Independent Expert**

Name	Company	Focus
Gerry Cross	Van Diemen Forestry Consultants Pty Ltd	Independent Forester

Gerry Gross has almost 40 years experience in plantations and forest industry management around the world, including 33 years experience in Australia, and holds tertiary qualifications in forestry. Gerry is a member of the Institute of Foresters of Australia and is a registered professional forester. In addition, Gerry is the Deputy Chairman of the Association of Consulting Foresters and is a member of Australian Forest Growers, National Association of Forest Industries and the Victorian Panel for the Accreditation of Forest Practitioners.

Adviser Edge conducted site visits on plantations in the Southern Slopes region of New South Wales on 28 November 2008, and Gunns Plantations' north-west Tasmanian plantations on 1 December 2008. Gunns Plantations' Operations Manager, Robin Dickson, accompanied Adviser Edge on both visits.

### **Southern Slopes, New South Wales**

Gunns Plantations is relatively new to the Southern Slopes region, with its first plantations established in 2006. Relative to Gunns Plantations' other plantation regions, the size of the holdings is relatively small, with approximately 2,800ha of softwood plantations in the region. This reflects a fairly cautious approach when moving into new planting regions.

The site visit illustrated the difficulties associated with establishing softwood plantations in dry conditions, with the 2006 and 2007 plantings having suffered higher than expected mortality rates as a consequence of dry conditions immediately after planting. These plantations have since been replanted in accordance with the PDS stocking guarantee, although the delayed start is expected to affect the ability to reach yields within the projected rotation period. Gunns Plantations has since implemented techniques to improve the survival of newly established plantations in an effort to minimise initial losses, and Adviser Edge is confident that these techniques will improve survival counts in the future. Nonetheless, the plantations in the region appeared to be very healthy, exhibiting dense dark green foliage and strong growth on established trees.

### **North-west Tasmania**

The site visit to north-west Tasmania demonstrated the extensive resources and infrastructure established by Gunns Plantations in Tasmania, together with the strong growth rates achievable in the region.

A tour of the Somerset nursery and the Gunns veneer mill demonstrated Gunns' commitment and expertise as an integrated forestry business, and a visit to the 2000 and 2001 plantations demonstrated the region's capacity to achieve high growth rates. However, Adviser Edge expects that average growth rates of the later, larger MIS projects will not have out-performed to the same extent as the 2000 and 2001 projects.

### **Planting regions**

Gunns Plantations intends to establish the plantations for Option 1 and Option 2 in Tasmania, and the plantations for Option 3 in both Tasmania (60%) and in the Southern Slopes region of New South Wales (40%).

#### **Tasmania**

Gunns Plantations intends to establish hardwood plantations under Option 1 and Option 2, and a majority of the softwood plantations under Option 3, in various regions of Tasmania.

The northern Tasmanian regions generally experience a cool maritime climate with mild summers and cool, wet winters. Rainfall is winter-dominant, ranging from 800mm to in excess of 1,000mm per annum. This area is characterised by deep and fertile soils, which are considered ideal for forestry plantations. The southern Tasmanian regions experience a cool maritime climate consisting of cool summer days and relatively mild winters. Rainfall is variable across the region, ranging from 550mm to 920mm.

Tasmania has a large timber industry with extensive resources along the forest products value chain. Gunns owns a forestry seedling nursery located in Somerset, manages approximately 141,000ha of predominantly hardwood plantations mainly in north-west Tasmania and north-east Tasmania, owns export woodchip facilities located in Burnie, Tamar and Triabunna, and operates a number of timber sawmills and veneer mills located around Tasmania.

Adviser Edge estimates that approximately 130,000ha of plantations have been established in Tasmania by different MIS companies. Other important agricultural activities in Tasmania include livestock (sheep, dairy and beef) and horticultural production.

### ***Southern Slopes region, New South Wales***

Gunns Plantations intends to establish the balance of the Option 3 softwood plantations in the Southern Slopes region of New South Wales. This region is located approximately 450km south-west of Sydney on the southern slopes of the Snowy Mountains. The main agricultural activities in this region are softwood plantation forestry and beef cattle farming. The main softwood plantation manager in the region is NSW State Forests, with Willmott and Gunns also having plantations in the region. The major end-user in the region is the Visy pulpmill and cardboard factory, as well as three major sawmills in the Tumbarumba region.

The region experiences mild summers and cool winters, with snowfall occurring at elevated heights. Frost events are also very common during the autumn, winter and spring months. Average rainfall is variable across the region, ranging from 300mm to over 1,200mm per annum, most of which occurs during the winter months. The higher rainfall sites are generally located closer to the mountains and further south towards the Victorian border.

### **Site selection and land availability**

Gunns Plantations has already secured the land required for the Project. In Tasmania, the regional split for the Project is as follows:

- 41% in north-east Tasmania
- 24% in south-east Tasmania
- 35% in north-west Tasmania

The majority of these sites are second rotation sites. These sites will either have yield data available to Gunns Plantations from the previous harvest or, inventory measurements undertaken on properties to be harvested in the next 12 months. , Where appropriate, Gunns Plantations has also utilised soil pits to assess soil depth and type, soil tests, previous land use history and advice from a Forest Practices Officer to ensure that a plantation can be developed under the Tasmanian Forest Practices Code. Adviser Edge has received yield data on some of the second rotation sites to be planted. While it is difficult to use this data to interpret potential yield for future rotations, it appears the yield data, together with the independent forester's review of the properties, demonstrate the potential of the land, as a whole, to meet yield objectives.

### Species and varieties

The Gunns Plantations Woodlot Project 2009 is comprised of the following species:

- Options 1 and 2: shining gum (*Eucalyptus nitens*) and Tasmanian blue gum (*Eucalyptus globulus*)
- Option 3: radiata pine (*Pinus radiata*)

### Options 1 and 2

The species to be planted for Options 1 and 2 will be predominantly shining gum, with a small proportion of Tasmanian blue gum. Shining gum is a preferred species for many sites because it is generally less prone to disease and insect attack, and it is relatively tolerant to frost. Its pulping characteristics are also well understood. Tasmanian blue gum is widely grown for short-rotation pulpwood plantations in southern Australia, and has ideal fibre characteristics for producing the Kraft pulp used in the manufacture of fine writing papers. Tasmanian blue gum will be grown on suitable sites, which are generally the milder, coastal areas. Tasmanian blue gum produces high yields of short, uniform wood fibres. The wood fibre is smooth and opaque, and the pale nature of its chips means that less processing is required for producing paper.

The seedlings for the Project will be grown at Gunns' seedling nursery in Somerset. This nursery is centrally located and within close proximity to Gunns Plantations' north-west plantation estate, and is close to the main highway between Burnie and Launceston. This nursery has expanded its capacity to approximately 20 million seedlings per year. The nursery grows a range of tree species, mainly shining gum and radiata pine, as well as some Tasmanian blue gum. The nursery has also grown vines for Gunns Plantations' previous winegrape projects.

The nursery is designed in a similar way to facilities located in Holland. The nursery design allows the seedlings to be moved around the nursery in the most efficient manner. The nursery operates with four full-time staff and up to 20 part-time workers during peak times.

***Shining gum and blue gum are well known plantation species, with well-documented growth potential and wood characteristics.***

### Option 3

Radiata pine will be used as the species for Option 3. Radiata pine is the most widely planted softwood species in Australia, accounting for an estimated 75% of all softwood plantations. This species is well suited to the cooler temperatures and higher rainfall of Tasmania and southern Australia. Gunns Plantations sources its softwood seedlings for both the New South Wales and Tasmanian plantations from its Somerset nursery.

***The growth performance of radiata pine is well supported, with a large base of technical knowledge available on the species.***

### Site development and stand management

#### Options 1 and 2

Site development works are carried out by a large network of contractors that Gunns' has developed over the years. The regime employed will depend on individual site characteristics and whether the site is a greenfield or second rotation site.

Greenfield sites will generally follow a process of clean up, knock down herbicide spray and cultivation, involving ripping and mounding. Gunns uses a strategy of ripping along the contour to improve water retention on the sites, although this practice needs to be balanced with the needs of an orderly site for efficient harvesting. Prior to planting, the mounds will be sprayed with a knockdown and residual herbicide to minimise weed germination.

On second rotation sites, Gunns will use spot cultivators mounted on an excavator, as conventional cultivation is difficult due to the presence of stumps from the previous rotation. Large debris will be swept into windrows, which will progressively decompose and add organic material to the land over time. The second rotation sites will also be sprayed using knock down and residual herbicides prior to planting.

Gunns will manually plant seedlings at a density of 1,100spha over the planting period from May through to December, although actual planting will be dictated by soil moisture conditions on the property.

The plantations will also be thinned at approximately age nine to promote growth of the remaining stand. The intention is to remove approximately a third of the standing volume at the time of thinning. Clearfall harvest is scheduled for when the trees reach approximately 13 years of age for Option 1, and 20 years of age for Option 2. A pruning regime will also be used for Option 2 plantations, with pruning lifts scheduled at four, six and seven years of age.

As part of the site visit, Adviser Edge visited the Surrey Hills property, which supports a large proportion of the Gunns Plantations' estate. Surrey Hills is approximately 80,000ha in size, of which approximately 40,000ha has been established as plantations. This property had a number of different age classes, with parts of the property under second and third rotation. These sites demonstrate Gunns' expertise in establishing and developing plantations on second and third rotation sites. The second rotation sites generally have lower weed issues when compared with first rotation sites due to a lower seed bank in the soil. Although the recently-established second rotation sites had a large amount of woody weeds, Gunns indicated that this was not a major issue as the woody weeds use less nutrients and water than grass species.

### **Option 3**

Site development processes for softwood plantations are very similar to hardwood plantations, with the sites being ripped and mounded and herbicide sprays being applied prior to planting. However, in the Southern Slopes region, it is Gunns' practice to rip but not mound the sites, to assist in soil moisture retention at planting. Mounding is used to create a raised soil bed, which encourages root penetration, minimises waterlogging, reduces the impact of frost, and assists in minimising weed growth. However, these factors are not considered to be a major issue with softwood plantations, as radiata pine is considered to be frost tolerant and the expected topography of the land indicates that waterlogging will not be an issue.

Planting densities for softwood are slightly higher, at 1,333spha and two commercial thinning operations are planned when the plantation reaches 13 and 18 years of age. Clearfall harvest is scheduled for when the trees are approximately 25 years of age.

On the site visit, Adviser Edge inspected properties planted in 2007 and 2008 in the Southern Slopes region. The Gillies property (2007) demonstrated the importance of soil moisture, with lower than planned survival rates on the property. The property has since been replanted to the required tree density. The visit to the Hardy property (2008) demonstrates the impact of Gunns' revised establishment regime for the region, with good survival rates for the 2008 planting. Both properties exhibited good growth, with healthy plantations and good weed control.

### **Harvesting and processing**

The harvesting method to be employed will be at the timber purchaser's discretion. It is expected that the timber purchaser will be Gunns, as stipulated under the Wood Sale Agreement. Gunns Plantations will determine the timing of the harvest based on the best interests of investors. Gunns currently contracts around 80 harvesting contractors to undertake harvesting operations on Gunns' behalf.

For Gunns Plantations' Tasmanian plantations, Gunns' owns and operates a number of wood processing facilities, saw mills and veneer mills capable of processing the timber from the Project. Gunns' export facilities are at Bell Bay, Burnie and Triabunna. The chipping facility is located on site at Bell Bay and Triabunna, while at Burnie the chipping occurs at the Hampshire Mill, which is located approximately 20km away. The combined capacity of these facilities is five million tonnes per annum, which is sufficient to meet the Project's needs.



### Market Overview

Product type	Eucalypt hardwood timber
Primary use	Pulpwood
Key target market	Domestic, Japan, and China
Major competitors	Domestic and international pulpwood and sawlog producers; substitute products

### Industry

The Australian forestry industry currently supports over 883,000ha of hardwood plantations, which are predominantly grown under short-rotation regimes (less than 12 years) for the production of pulpwood to be used in the pulp and paper industry. Taxonomically defined as angiosperms (flower bearing trees), hardwood species currently account for approximately 46% of Australia's total plantation area. Approximately 600,000ha of Australia's current hardwood plantation resource has been established under managed investment schemes (MIS), with the majority in Western Australia, Tasmania and Victoria. Due to an increase in MIS activity, the rate of new hardwood plantings has increased significantly over the past decade. For example, 76,057ha of hardwood was established in 2007, compared to approximately 31,400ha in 2003. (Australian Plantation Inventory Update 2008)

Australia harvested approximately 12.5 million cubic metres of hardwood in 2007, of which 4.0 million cubic metres (32%) were sourced from plantation resource, with the remainder from native stands.<sup>1</sup>

In the longer-term, the rate of new forestry development is expected to slow as green-field development declines and second rotation land becomes available. However, because of the high rate of hardwood plantation development in previous years, it is expected that hardwood timber production, particularly that of woodchips, will increase significantly in the coming decade. In terms of total Australian hardwood production, a decrease in native harvesting may offset some of these increases.

The Commonwealth Government of Australia has taken initiatives to promote plantation forestry in Australia through the Plantations 2020 Vision. Its objective is that, by 2020, the total Australian plantation forestry estate will reach three million hectares. To achieve this level, the industry must plant over 80,000ha of new plantation forests each year until 2020. While this target seemed quite achievable in 2004 and 2005, the competition for land with other land-use industries, and the subsequent increases in underlying land value, has significantly

### Key Points:

- Japanese pulp and paper manufacturers are the key market for hardwood woodchips for Australian growers. However, the Chinese market is expected to increase over the next decade, either directly through woodchip demand, or indirectly through pulp demand.
- Australian plantation woodchip exports are forecast to increase as current MIS plantations mature.

reduced the affordable land area viable for short rotation forestry. This is particularly noticeable in the temperate areas of Australia. The development of tropical forestry, and a shift in focus to long-term regimes targeting solidwood, is expected over the next few years.

### Market overview

Most plantation hardwood fibre produced in Australia is destined for the pulpwood market as woodchips, with the majority exported. Declining domestic demand for hardwood as a whole, combined with the rapid increase in the area of hardwood plantations, has resulted in the industry becoming increasingly focused towards export markets for woodchips. Hardwood woodchips are a major export earner for Australia, generating \$1.07 billion for the economy in FY2007-08. This represents approximately 43% (by value) of all exported timber products.

Europe and the Asia-Pacific region are the two key global markets for pulpwood trade, with Australian hardwood woodchips currently sold almost exclusively into the Asia-Pacific region. The major markets for Australian hardwood woodchips are pulp and paper manufacturers in Japan, South Korea, China and Taiwan.

Japan has traditionally dominated the Asia-Pacific woodchip trade, consuming nearly 90% of the pulpwood traded within the region. South Korea and Taiwan are the other major pulpwood importers, with China set to emerge as a net importer over the next decade. The current market dominance of Japan is reflected in Australia's woodchip trade, with 91% of Australia's hardwood woodchip export volume shipped to Japan in 2007. (ABARE Sept-Dec 2007)

Japanese importers are able to pay premium prices for woodchips because of their unique and highly protected paper markets. Japanese pulpwood buyers operate under a framework which stipulates that one third of their pulpwood requirements must be sourced from natural forests and two-thirds from plantations. Of these two-thirds, one third, or around 22% of total pulpwood requirement, is to come from Japanese-owned plantations overseas, and the remainder, 44% of the market, is

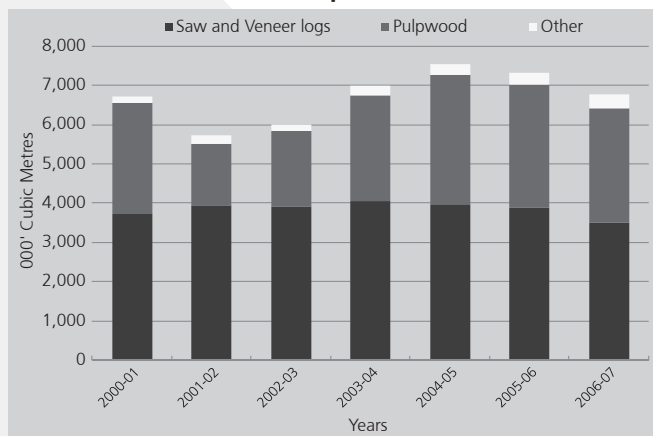
<sup>1</sup> Native stands can be distinguished from plantations by the planting and management techniques used.

available to foreign owned plantation supply. In 2007, approximately 78% of Japanese woodchip imports were sourced from plantations.

Australia exported 4.75 million BDMT of hardwood woodchips to Japan in 2007, accounting for approximately 37% of all Japanese imports. Other major exporters of woodchips to the Japanese market include South Africa (21%), Chile (17%) and Vietnam (8%). (RISI 2008) Of the hardwood woodchips that Australia exported to Japan in 2007, approximately 50% were sourced from plantation resource, compared to just 2% 10 years earlier.

Saw and veneer logs produced in Australia are generally consumed for domestic purposes, and have traditionally been sourced from native forests. However, the harvest of these resources is becoming increasingly restricted due to the reduction of native harvest quotas by many state governments. The domestic high quality veneer market also relies on resources from native forests, to which access is also becoming increasingly restricted. The following graph illustrates the Australian consumption of hardwood logs for its intended uses.

**Australian domestic consumption of hardwood**



**Market outlook**

While Japan remains the major importer of woodchips in the Asia-Pacific market, China is an emerging market with solid demand in paper, board and panels. China sits well below most developed nations in per capita paper consumption, but with high GDP growth forecast to continue for the next five years, Chinese consumers can be expected to become significantly higher paper users. This is likely to have a direct impact on the global trade of hardwood woodchips. China’s capacity to import woodchips may be limited by the rate of development of new pulp mills, as well as its ability to compete in open woodchip markets, and it will probably seek to increase pulp imports from Japan. The forecast growth in Chinese markets remains positive despite the global financial problems.

The Australian plantation hardwood industry continues to prosper in terms of new plantings and investment, although growth is expected to plateau in the near-term. As plantations mature and harvests increase, the importance of developing and retaining key Asian markets for woodchips will be paramount. The profitability of the industry, particularly with respect to MIS investors, will be dependent on improving production efficiencies as well as retaining and increasing the current market share in Asia-Pacific markets.

The price outlook for plantation hardwood chips is also influenced by key factors such as currency volatility, the profitability of pulp and paper companies, and competition from other exporting countries. As the supply of plantation timber increases over the long-term, the premiums paid for plantation woodchips may decrease.

***For these reasons, Adviser Edge considers it important to retain a conservative view of the long-term price outlook for plantation hardwood woodchips.***

Australian woodchip exporters retain significant competitive advantages over other nations in the Japanese market due to their proximity, with shipping times of between 16 and 18 days from temperate Australia, compared to 30 from Chile and 25 from South Africa.

Concerns regarding the possibility of an oversupply of hardwood woodchips are offset by the potential for increased exports into the Asia-Pacific market. Nonetheless, it is important to note that the Japanese market is expected to mature in the next decade, and with the major increase in supply from Australian plantations it will be important to explore additional Asian markets.

As supplies of Australian native hardwood become increasingly limited, the demand for hardwood sawlogs and veneer logs will turn to plantation derived resources. However, to date few clear grade hardwood plantation regimes (the target grade for Option 2) have been established in Australia. As such, it is expected that the supply of Australian-sourced clear grade logs and laminated veneer products will remain constrained. Historically, the overwhelming majority of the laminated veneer products manufactured in Australia have been consumed domestically. It is expected that the domestic market will remain the key target market for clear grade wood products in Australia, although there is potential for the development of export markets.

**Compliance**

While the woodchip export industry has historically relied on native forest timber, these woodchip markets are starting to show a preference toward ethically and environmental accredited plantation woodchip resources. Two recognised forestry accreditation systems currently exist in Australia: the

Forest Stewardship Council (FSC) and the Australian Forestry Standard (AFS). At present, there is little evidence to suggest that a price premium can be obtained from forestry accreditation. However, many export customers are indicating a preference for certified products, and it is possible that in the future a premium could be obtainable.

To further substantiate the sustainability credentials of plantation timber, chain of custody certification can be obtained to the Australian standard (AS4707-2006). This certification provides users with certainty regarding the origination of the product as it moves through the value chain.

***Gunns has an Environmental Management System in place which is accredited to ISO 14001 and the Australian Forestry Standard. These accreditations are verified and audited by Det Norske Veritas to ensure on-going compliance.***

**Market Overview**

Product type	Softwood timber
Primary use	Sawlog and pulpwood
Key target market	Domestic
Major competitors	Domestic and international softwood producers

**Industry**

The majority of softwood grown in Australia is radiata pine (*Pinus radiata*). This species is favoured for its ideal workability and its compatibility to preservative treatments. Radiata pine is generally grown in a 25 to 30-year rotation, and the timber is mostly used in the building and furniture industries. Australia currently has about one million hectares of softwood plantations, mostly established in higher rainfall areas of New South Wales and Victoria.

The volume of softwood sawlogs being harvested in Australia has increased strongly over the last 15 years. The total softwood harvest in FY2006, as measured by roundwood removals, was estimated at just over 14.2 million cubic metres. This represents a 115% increase on FY1991, when an estimated 6.6 million cubic metres was harvested. It was estimated that slightly more than two-thirds of the softwood timber harvested in FY2006 was used for sawn wood applications. The balance of this resource was used to produce pulpwood.

**Market overview**

Radiata pine logs are generally sold as pulpwood or sawlogs in Australia. Pulpwood is mainly used in the manufacture of rough papers such as newsprint and kraft liner for cardboard manufacture, although it can also be used to produce manufactured wood products such as medium density fibreboard (MDF) or particleboard. The majority of softwood pulpwood produced in Australia is processed for domestic use.

Softwood sawlogs are processed into a wide range of timber grades, the most important being the structural grades. The majority of structural grade timber sold in the Australian market is sourced from softwood plantations (mainly radiata pine). Most softwood sawlogs that are produced in Australia are processed and consumed domestically.

**Market outlook**

Australian softwood sawn timber consumption is driven largely by building construction rates, and is therefore related closely to population growth and the strength of the prevailing economy. Economic conditions will fluctuate considerably over the term of this project, and it is possible that the market for softwood will be weak at the time the plantation is sold, thereby affecting prices. Although the real prices for softwood have been declining in recent years, the softwood resource has remained

**Key Points:**

- The majority of softwood produced in Australia is processed for domestic use
- The Australian softwood resource is expected to remain relatively static over the next 20 years
- Historically, the price for softwood products has been distorted by the prices paid under long-term government contracts

and is expected to remain relatively static for the next 20 years, at around one million hectares.

Due to high transport costs, Australian domestic softwood producers have traditionally been able to compete with imported softwood producers. New Zealand poses the biggest threat of competition, being the largest exporter of forest products (in terms of value and volume) into Australia. Canada is also a large exporter of softwood products into Australia, but the level of imports from this country has generally declined in recent years. Historically the New Zealand industry has supplied the Australian market with products not available in the country, including treated structural timber and clear timber. While there is scope for Australian timber mills to focus on producing timber for these markets, the industry is currently limited by processing infrastructure suited to this timber.

The long-term contracts that exist in relation to government owned plantations have particularly affected the softwood industry. These contracts have resulted in artificially lower log prices, which do not adequately reflect the relative scarcity of the softwood supply. In order to promote softwood prices that reflect the value of softwood timber, these administratively-priced contracts need to expire and/or be reviewed. Also of concern is the increasing consolidation of the softwood processing industry, which has occurred as a consequence of the lower sawn wood prices. Should these structural issues be addressed, the long-term market dynamics indicate a positive outlook for softwood in Australia.

The following section provides a more in-depth discussion of the key project parameters outlined in the main report.

## Hardwood Pulpwood and Woodchip Price

### Hardwood woodchip and sawlog price trends

The FOB price received for Australian hardwood woodchips is determined by a variety of factors, including the prevailing market supply and demand conditions, exchange rates, production costs, transport costs, and the prices offered by competitor countries.

The hardwood plantation woodchip export industry is relatively young in Australia, with export volumes only beginning to increase over the past five years. Based on the development of short rotation hardwood plantations, the export volume for plantation woodchips is expected to climb significantly over the next decade. As such, a study of the industry trends for native hardwood woodchip exports is the best way to assess the long-term trends for plantation woodchip export prices. The average FOB export price for native woodchips is based on the price paid by Japan for non-plantation woodchips shipped out of Tasmania by Australia's largest woodchip processor, Gunns. This price is referred to as the Leading Australian Hardwood Chip Export (LAHCE) price, and is used as a benchmark for Australian hardwood woodchip industry exports.

It is important to note that the LAHCE reflects the price being received by exporters of native woodchips, with many forestry industry practitioners believing that the pricing mechanisms for plantation-grown woodchips are beginning to operate independently. This change may develop further as more plantation resources enter the woodchip export market.

The LAHCE has increased by approximately 29% in nominal terms over the past eight years, from \$143/BDMT in 2000 to \$184.50/BDMT in 2008. However, this represented an increase of just 2.5% in real terms over the same period. Many industry experts believe that the real price trend for woodchip exports is likely to continue as it has done in the past. However, some of the more optimistic industry participants believe that the global supply/demand imbalance between pulp production and paper demand is likely to favour high global woodchip price increases.

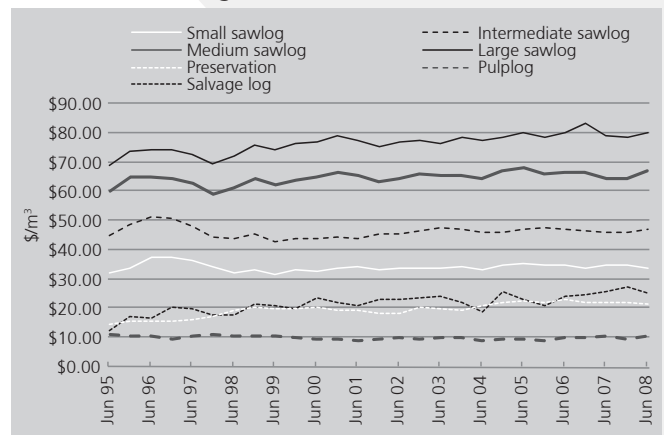
The Australian woodchip industry was able to negotiate an increase of approximately 10% in plantation and native woodchip export prices in 2008, after a number of years of only nominal price increases. This large increase is thought to be the beginning of a resurgence in woodchip export prices, reflecting the supply/demand imbalance caused by China's increasing appetite for affluence. However, recent turmoil in global financial markets has caused a decrease in China's economic growth rate, and a number of importers have reportedly reneged on their contracted commitments.

## Softwood Pulpwood and Sawlog Price

### Softwood price trends

Domestic softwood log prices are monitored by the Australian Pine Log Price Index (APLPI), which is compiled by KPMG, and based on data provided by the largest softwood growers in the eastern states of Australia. Updated every six months, the APLPI follows sales prices of common grade softwood logs to domestic processors, relative to the index base period of January to June 1998. The index does not necessarily reflect regional prices obtained, as domestic prices can vary significantly both between and within geographical regions. The following graph illustrates price trends for the sale of common grade softwood logs to domestic producers since 1995.

Australian Pine Log Price Index



The real price for the four most expensive grades of softwood logs (small, intermediate, medium and large sawlog grades) has fallen over the last decade. This is despite the price of housing material accelerating over the same period. The nominal price received for large sawlogs has increased by the largest margin in the last five years (11.6%), which is still less than the rate of inflation over the period. Nominal prices for medium and small sawlogs have increased slightly in the last five years, while the price received for intermediate sawlogs has retreated by 1.3% in this period. The price received for softwood pulp log has also fallen in real terms over this period.

Market experts believe that administrative pricing mechanisms used by the state governments, the largest growers of softwood plantation resources, help to distort and undervalue the real market price of radiata pine logs. (IndustryEdge 2008) The distorted market has resulted in current softwood log prices being below world parity. A contributing factor to the weakening prices trends for sawlogs is that only a small number of major softwood processing companies operate in Australia, which means that competition for softwood resources is limited.

It has been forecast that the domestic supply of softwood resources will only increase slightly in coming years, which may

lead to regional shortages in some areas. Given the potentially static supply of softwood timber, and a declining supply in structural timber sourced from native hardwood stands, it is anticipated that processors may be prepared to pay a premium to guarantee supply.

Investors in the Gunns Plantations Woodlot Project 2009 will be subject to risks associated with medium-term forestry investments. All potential investors should carefully consider the risks outlined in the project PDS, and the specific risks outlined in this summary document and the Adviser Edge research report.

### **Management risks**

MIS management encompasses not only the operational capabilities of the project counterparties, but also the corporate abilities of Gunns Plantations to monitor operational performance, and meet the regulatory and statutory responsibilities required of it as Project RE. For all MIS projects there is a risk that if the financial position or performance of management deteriorates, asset condition, project outcomes and/or regulatory outcomes may be temporarily or permanently compromised.

### **Structure and fee risks**

Ongoing management and lease fees are deferred and taken as a percentage of harvest proceeds. The fee structure means that investors have some protection from unexpected increases to plantation management costs over the Project term.

### **Site and silviculture risks**

Investors should be aware of the risks associated with the site and management of the Project. Four key areas of risk identified by Adviser Edge are:

#### ***Site selection***

This is a risk that the selected land is not suitable for the selected species. This risk is mitigated by the fact that Gunns Plantations has already secured the land required for the Project.

#### ***Pests and weeds***

Insect damage can adversely affect yield. Weeds can also affect growth rates through competition for water and nutrients, and may act as a vector to unwanted insects or diseases.

#### ***Infrastructure***

Infrastructure risks include the factors associated with transportation, processing and skilled labour. Infrastructure in Tasmania and the Southern Slopes region of New South Wales is well developed, and access to domestic and export markets is clearly defined.

### **Performance risks**

#### ***Yield and quality***

Activities that deal with forestry are exposed to similar risks as those inherent in other agricultural production systems. Risks relevant to the plantation forestry industry include the impact from climatic events such as low rainfall, excessive heat and wind, and seasonal aspects such as fire, pests and diseases. Investors should be aware that even conservative yield estimates are prone to failure due to adverse growing conditions. However, these threats can be mitigated by good site selection.

### ***Information risk***

This is the risk that the productivity assumptions used are too optimistic or that the productivity potential of a selected property is overestimated. This risk is mitigated by the fact that Gunns Plantations uses a large proportion of second rotation sites, on which the yield potential is easier to determine.

### ***Price and costs***

Investor returns will be directly affected by pulpwood and sawlog prices, and the costs of harvesting and processing. While prices and costs are generally dictated by the dynamics of supply and demand, changes in certain macro-economic factors can also have an impact. Such factors include exchange rates, interest rates, and inflation. Investors need to be aware that these factors can negatively affect Investor returns.

### ***Marketing risks***

As with any MIS project, there is a risk that the market for the Project resources will encounter a significant downturn at the time of harvest. This may be due to factors such as competition, regulation and/or market preferences. The effect of reduced demand may affect resource prices, which could potentially reduce investors' returns.

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