The outlook for plantation ownership by Māori

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Introduction

The potential for Māori to grow their share of both plantation land and tree ownership is sometimes held up as a beacon of hope for increasing domestic involvement in the industry. From a national perspective greater Māori involvement in the industry would probably be beneficial. Māori permanence on and deep connections with their lands are consistent with the long time horizons required for forestry, and the bulk of any profits generated are likely to stay in New Zealand. For Māori too it could lead to long-term benefits. In addition to any financial returns, it would help sustain their connection with their lands, generating employment and supporting the rural communities in which many prefer to live.

Forest trustees discuss operations with contractor

This paper assesses the likelihood of increased plantation ownership by Māori and looks at some of the factors which will influence this. A paper about Pakeha and forestry may be considered facetious and unlikely to find its way to print. Similarly, this paper on Māori and forestry is not an inference that Māori have a single opinion on or approach to the industry. Each situation is different, and within each land-owning group there will be divergent views on whether an investment in forestry on their own lands should be pursued.

Current plantation and plantation land ownership

Change has been a characteristic of much of New Zealand's plantation ownership over the last 25 years, and with the dominance of Timber Investment Management Organizations (TIMOs) in our industry we can expect this to continue. Prior to the state forest sales of the 1980s and 1990s, virtually all of the country's 1.1 million hectares of plantation forests were domestically owned. The state owned around half of this area and a further 25 per cent was owned by three large domestic companies. Today over half of the nation's 1.7 million hectares of plantation forests are owned by foreign entities, including 80 per cent of the area in large (greater than 10,000 hectare) forests.

The largest domestic owner of plantations is again the state, with about seven per cent of total ownership. This comes through the NZ Super Fund's 41.25 per cent share of the 176,000 hectare Kaingaroa Forest and the Ministry for Primary Industries' Crown Forestry Group which currently administers 46,000 hectares. Plantation forest land ownership has also experienced change. Through the Treaty settlement process large swathes of plantation land have been returned to Māori ownership, rapidly increasing their status as forest landowners. This trend will continue as settlements are processed, although it is likely that once the land is in Māori ownership it will remain so indefinitely.

The largest Crown forest land settlement has been the 176,000 hectare Central North Island settlement, completed in 2008, but many others have occurred. To date the Crown has returned to Treaty claimants around 260,000 hectares of Crown forest lands and a similar area remains potentially available for settlement. While statistics around Māori land ownership and land use are notoriously unreliable, in addition to the Crown forest lands there is an estimated 70,000 hectares of plantations on land leased from Māori owners, plus a further 80,000 hectares of forests owned by Māori on Māori land.

In total, there are currently around 420,000 hectares of plantation forests on Māori land. By the end of the Treaty claims process this may increase to around 680,000 hectares, or 40 per cent of the country's plantation estate. Māori currently own around 80,000 hectares of plantations of which two entities own half – Ngai Tahu (in the process of completing due diligence on the 24,000 hectares of former Timberlands West Coast forests) and the Lake Taupo Forest Trust. Under confirmed intentions, by 2030 this area may increase to around 110,000 hectares, or six per cent of New Zealand's total planted area.

Lease arrangements

Crown forest land leases provide the lessee up to 35 years to complete the harvesting on the land, although most land is likely to be surrendered within around 30 years. The claimants continue to receive annual rental payments, although unless the lease is extended or renewed, these payments will steadily reduce as trees are harvested and the bare land is surrendered from the lease.

The period from the mid-1960s to the late 1980s saw numerous Māori landowning trusts lease their lands to the Crown and to private forestry companies. The terms of the leases generally provided for one, two or three rotations of pine trees, with landowner income paid through an annual rental, a stumpage share, or a combination of the two. Conditions on some leases require that the outgoing lessee replants the land before it is surrendered. In these instances the expensive up-front establishment work has been paid for, and the Māori landowners are likely to continue to maintain ownership of the forest, at least until the end of that rotation.

Challenges to Māori forest investment

Owning the lands on which plantations are grown opens up for Māori relatively straightforward pathways to move to tree ownership, but how likely is this to occur? Closer analysis of the challenges facing Māori landowners indicates that the step from landowner to tree owner will often continue to be a difficult one.

Cashflow challenges

As all journal readers will realise, investing in forestry requires deep pockets, entailing significant expenditure for 25 to 30 years before returns are generated and during which the liquidity of the investment can be poor. From an emissions trading scheme perspective, most plantations on Māori land are pre-1990, although there is potential to create post-1989 forests on low productivity farmland. While the carbon income generated will help cashflow, the performance of this sector to date has clearly been insufficient to encourage such investment from Māori or any other investor.

If Crown forest land is available, it provides a significant commercial redress under a Treaty settlement. A settling iwi has the option to purchase this land with their cash settlement. This land is very appealing to the iwi as it brings with it substantial forestry rentals that have accumulated each year and been held in trust by the Crown Forestry Rental Trust since around 1990.

Those responsible for managing these funds are obliged to weigh up the many ways in which this capital can be used. Iwi members will have a wide range of suggestions, likely including various business investments, and cultural initiatives such as grants for health, education or marae development. Long-term cashflow planning is essential, balancing investments not only on their expected returns but also on the expected timeframes. Ideally a mixture of short, medium and long-term investments may eventuate.

In light of these competing desires, iwi fund managers may conclude that a forestry investment that demands an extended period of expenditure, with little or no prospect of returns for 30 years, may simply be unacceptable. Certainly to date there have been few examples of accumulated rental funds being allocated to replanting on claimed lands.

By continuing to lease their lands and receive rent, Māori are guaranteed an ongoing and largely risk-free annual cashflow. This reliable income forms a useful basis from which to plan and facilitate an investment strategy from which iwi members can expect to start seeing meaningful returns within acceptable time horizons. A move from landlord to forest owner will, in the short and medium term at least, compromise this.

Landowners working in harvesting gang

Most Māori organisations are fairly conservative in their approach to investment, and will be reluctant to go into debt. While taking on debt makes financial sense for short-term investments, the business case for debt loading is more challenging for forest investments owing to the long periods of negative cashflow. A compounding barrier for many Māori landowners is their inability to use their land for collateral to raise investment funds.

In weighing up whether to invest in the next crop on leased land, Māori will realise that their ongoing rental income will be insufficient to cover the cost of a whole rotation. The graph below presents typical cashflows a landowner will face in attempting to resume full ownership of leased lands as the lessee departs over a 35-year period. It assumes any excess rental income from year 0 is held in reserve, earning a modest interest, for later use in the replanting and management programme.

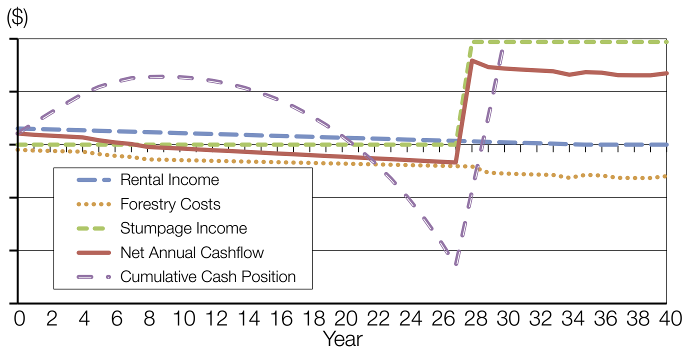

Figure 1: Typical cashflows for iwi attempting to resume a forest lease

Unless the landowners opt to commit a portion of their accumulated rental to such a project, the (steadily diminishing) rental from a departing lessee will be sufficient for a landowner to afford only a 50 to 80 per cent share of the subsequent rotation. If the land offers a reasonable forest investment it is likely that a co-investor can be found, although they may prefer at least a 50 per cent stake in the business. This therefore will not give the Māori landowner the control they may have sought as one of the primary reasons to invest in the first place, and will then require a 60-year commitment (two rotations) before they start receiving the full harvest income from their lands.

Kaumatua inspect their land and forest

A lessor wanting to resume a land lease and invest in the next crop will need to retain and manage their annual rental income from the outset. Retaining rental income over a full rotation is challenging for any investor. For iwi groups, there are likely to be even more pressures on income from iwi members which require strong leadership and discipline to resist.

Interestingly, this transition can be considerably easier to achieve when the initial lease arrangement allows for a share of stumpage rather than an annual rental. It does not however represent a free lunch. It appears to be easier only because the landowner will by then have gone without income for (say) 25 years while waiting for any stumpage to be generated, in effect a forced savings scheme. Once harvesting commences the annual income from stumpage will be considerably higher, typically around four times greater than the rental income.

By definition it is coming at the same time that it is needed for the replant, so less discipline is needed to retain the funds for this purpose. Depending largely on their stumpage share, and the profitability of the forest itself, the landowner may be able to afford to commit to the full replant and management of the next rotation and possibly even have something left over for distributing.

The Lake Taupo and Lake Rotoaira Forest Trusts, who formed stumpage sharing leases with the Crown in 1969 and 1973 respectively, are in the process of following this model. While there is little spare money during the transition years, their stumpage shares from the first rotation are sufficient to cover the costs of establishment, silviculture and associated management of the second rotation crops which they will commence harvesting in the early to mid-2020s.

Financial returns from forestry

Most commentators within the industry seem cautiously optimistic about the outlook for global wood markets and the economic prospects for the type of plantation forestry practised in New Zealand. Real returns of five to seven per cent are often forecast from investments on 'average' forestry land. However many forests earn far less and the overall profitability of plantation forestry is a concern for the industry.

Not surprisingly, we are not seeing much investment except from multi-billion dollar pension funds. The investment drivers for such organisations, seeking to put a small percentage of their portfolio into a steady investment like forestry, are very different from those of most Māori trusts and incorporations. Until the industry works out how to improve its returns (and if we are sticking with radiata that must mean ensuring more fibre gets turned into more valuable end products than concrete boxing and packaging), then Māori are likely to be no different from other investors in their reluctance to put money into tree ownership.

As Māori land is seldom sold, its market value is of less importance than the returns it can generate from its use. Māori land trust accounts often rely on land values determined for rating purposes, and these are often distorted as rating values reflect average market prices rather than the returns that can be achieved from working the land. Valuing forestry land at say $3,000 per hectare will indicate the return on asset value (land plus trees) may be only two to four per cent, while if the land value is assumed to be $1,500 per hectare the return on asset value may climb a few per cent.

If Māori want to generate returns from their lands they may be best to look at the cashflows generated and factor in the numerous other benefits from investing on their own lands, rather than targeting a hurdle return on asset value. Forestry will generally provide higher returns than pastoral use, possibly excepting dairy, but if ratings land values are used as a basis to calculate hurdle investment returns then off-land investments may be unfairly favoured.

Employment

For most Māori entities owning rural lands, creating employment for owners and their descendants remains a very important objective and continues to influence land use decisions. The communities around the lands are often largely populated by owners and their descendants, while work opportunities in these areas are limited. This in turn directly threatens the sustainability of these communities, and getting even a few people into reliable work can make a significant difference.

The Tuwharetoa Forest Trusts now provide marae grants

Many lessees and forest managers are quite understanding and indeed helpful regarding owner-employment, but being a landowner only will generally limit a Māori landowning entity's ability to influence who gets to work on the land. This in itself may be a significant driver in encouraging Māori to take a greater involvement in tree ownership.

The employment objective runs far deeper than simply giving owners a job. Cultural and spiritual links with the land need to be nurtured, and an opportunity to work on the land helps to facilitate this. Many owners also feel comforted by the knowledge that those working on the lands are also owners, knowing they will respect any wahi tapu, and indeed the entire whenua, in an appropriate manner.

There is also the recognition that distributions from the profits generated on these multiple-owned lands are ultimately unlikely to represent a living income for any individuals, so it is important that at least some of the owners are meaningfully (in a financial sense) benefiting from the arrangement.

Spreading risk

As owners of plantation land, Māori are exposed to the forestry business, regardless of whether they own the trees. Rental payments, and in some instances stumpage shares, are intermittently reviewed, and the outcome essentially revolves around the financial viability of forestry compared with other land uses at the time. There is generally a lag in the movement of land value as land use profitability varies, but there are interdependencies, so the value of the land will be related to the profitability of the forests grown on it and so in turn will be the rent paid for the use of that land.

With the land itself typically comprising a very large proportion of the Māori landowner or iwi asset base, those with plantation land have a considerable exposure to the industry. Iwi have to weigh up whether it makes sense to invest more of their limited funds in forestry by resuming the leases, or to spread their investments and reduce overall investment risk by targeting any surplus funds specifically toward non-forest investments.

Land characteristics

Considerable areas of Māori-owned land do not present an attractive forestry investment – being limited by terrain, fertility, location and/or altitude. This includes some Crown forest lands returned under Treaty claim, many of which were established foremost for environmental and land stabilisation purposes. In these situations the landowners may have difficulty in attracting a lessee, even at very low rental levels, while investing themselves will in effect lock them into a low-return investment.

Karakia at the start of a new harvesting operation

There are examples already of lands in Northland where the landowner has been unable to find an investor to replant following the expiry of the initial lease. In some instances the lands are reverting to scrub and with luck, possibly assisted by human intervention, will over a very long timeframe progress through to ecologically useful native forest. Fortunately for these landowners, the reversion of these lands appears to be meeting the emissions trading scheme reforestation obligations.

Fragmentation

In the case of Treaty settlement forest lands, in particular, there is likely to be a range of views among the claimant's constituent hapu as to whether to resume the land themselves or whether to extend/renew leases and continue taking an annual rental, or indeed to pursue a combination of the two. In larger claims, this may impact on the claimant's ability to maintain the forest area as a single forest management unit as some may prefer to take out those lands for which they have mana whenua and either make their own forestry arrangements or change the land use on that land.

From an economic perspective, the land will invariably present a more attractive forest investment if it can be managed as a single forest estate. Studies indicate that economies of scale are significantly improved if areas under management are 30,000 hectares or more. However lands returned under Treaty claim cannot be just thought of as squares on a map. There will typically have been centuries of occupation during which cultural and spiritual connections were established followed by generations of pain associated with its alienation. Understandably the descendants of the original owners will have a strong desire to re-establish their mana over the lands, with this potentially taking precedence over economic considerations.

Irregular land return

Under most leases it is the lessee's prerogative to decide when and where land will be returned. The only requirement is that it is all returned by a specified termination date, which is 35 years in the case of Crown forest lands. For larger forests, which may have achieved some degree of normalcy in age class structure, the area of land returned each year is likely to be reasonably regular. Even then the location of the various components of the land being returned may not lend itself to easy replant planning and ongoing management. The outgoing lessee has no compulsion to consider this in their harvesting plans.

In smaller forests (say under 5,000 hectares), initial planting was probably completed over a short timeframe (say 10 years) and the harvest and land return may occur over a similar period. In some situations, such as when harvesting is held over until more favourable market prices prevail, there may be gaps in the harvesting and in some years no land will be returned. This can cause further difficulties for the Māori landowner contemplating investing in the replanting, especially if employment is a key driver. It is difficult for owners to establish themselves as forestry contractors if their base workload has gaps lasting for years.

Overhead costs

Much like a corporate overhead, Māori landowning trusts and incorporations are expected to undertake a range of roles unrelated to the actual land use. Maintaining contact with what can be many thousands of landowners or beneficiaries, holding forums for discussion and decision-making, and arranging and policing landowner access are a few of the time-consuming and expensive tasks they are obliged to perform. Even larger Māori trusts can face non-forest overheads of over $70 per stocked hectare per year.

The role of lessor can be relatively straightforward and administratively efficient. It largely entails the collection of rental payments, with some on the ground monitoring only to check that the culturally important aspects of the lands are being respected, and decision-making around funds management. By comparison, a decision to venture into tree ownership will greatly increase the administrative workload and cost. Even if the actual management is contracted out, decisions have to be made about the general approach to the forest operation, contracts negotiated, owner employment initiatives advanced, work monitored and invoices paid.

Likely outcome

Māori are significant owners of forest land and will become more so over next 10 years as the major historical Treaty claims are settled. There are many issues for any organisation considering investing in forestry, particularly under the current climate, but Māori owners of plantation forest lands face some unique additional challenges. These include:

- Competing (social) demands on capital
- Lease exit mechanisms that often favour the lessee
- Lands which may present a marginal commercial forestry proposition
- The need to spread their investments given they are already highly exposed to the industry
- Competing ideas on how the lands should be used.

There are cultural reasons which may encourage Māori to invest in trees on their lands, including the desire to create employment for owners and to help maintain rural communities and connections with ancestral lands. However the above challenges, and indifferent returns from forestry in all but the best circumstances, indicate that such investment may be limited over the medium term. While Māori may own around 40 per cent of the nation's plantation lands by 2030, they may by then still only own around six per cent of its plantations. Interestingly this may provide tree investors, such as TIMOs, with some confidence in the stability of the model of investing on Māori-owned land.

The decision on whether or when to invest in trees on their lands however will remain under Māori control. Should the combination of internal factors (cashflow, employment, spreading risk) and external factors (returns from forestry) conspire to make tree ownership more attractive, Māori landowners will be able to commence such investment at short notice.

In the longer term, as Māori investment portfolios become larger and more diverse, an investment in tree ownership on their own lands may become both more sensible and achievable. Providing the industry itself can improve its profitability, this will be a positive result both for Māoridom and for the country.

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