



The Waterfalls Forest Investors' Story

How an initial investment of \$2,280 in 1973 is today returning \$151,506.

In 1973 25 people, mostly business people from Wellington and Wairarapa, formed Forest Enterprises first forestry partnership called Waterfalls. The partnership took its name from the original farm on which their 155 hectare (383 acre) forest was to be established in the Bideford district some 24 kilometres north east of Masterton.

This was probably the first public issue radiata pine forestry investment in New Zealand and many things were quite different from both the forestry and investment perspective. For a start, most of the land had to be cleared of gorse and scrub before planting and was therefore generally of a lesser quality than the mainly clear fertilized farmland selected today.

The treestocks used would probably rate about GF7 on today's GF (Growth and Form) rating system compared with GF19 and higher used today and consequentially have yielded less volume per tree. And although most of the trees were pruned to 6 metres, the final stocking at around 250 stems per hectare is much less than the 350 to 375 stems aimed for today hence the overall volume per hectare being harvested is about 30% less than what is expected from recent plantings.

The top marginal tax rate at the time was 46.25 cents and applied to income over \$12,000 equivalent to about \$106,300¹ today. Income of \$10,000 (equivalent to about \$88,600 today) attracted a tax rate of 45.325 cents. Forestry expenditure was not tax deductible in 1973 however the Forestry Grant Scheme was operating. Under this scheme the Government paid back qualifying forestry projects 50% of their previous years forestry expenditure as a contribution towards the next years expenditure.

Death duties (now abolished) were a huge financial worry for many in 1973 and an original attraction of the Waterfalls investment was undoubtedly the fact that standing timber was specifically exempt from the total value of ones estate at death.

It was in this climate that the Waterfalls investors each contributed \$2,280 in the expectation of receiving taxable income of \$29,750, a net return of \$16,623² after tax assuming a marginal tax rate of 45 cents. Expressed in 2002 dollars, each invested the equivalent of \$20,197.

The period from 1973 to the present has traversed some of the most tumultuous financial times in New Zealand's history. Between 1973 and 1986, inflation averaged a staggering 12.56% per annum, peaking in 1986 at just under 19%. For the entire 30 years from 1973 (including almost 12 years of price stability under the Reserve Bank Act) the average inflation rate has still been a surprising 7.54% per annum. To complete the picture, add an international oil crisis plus a share market crash.

So what return are these pioneer investors actually currently receiving? Firstly we have to acknowledge that their original investment of \$2,280 ran out in 1980, having been eroded by inflation and they ended up investing a total of \$14,380. Projecting the harvest outcome to date across the entire forest, each investor is on target to receiving \$151,506 gross, which at a marginal tax rate of 33 cents will net \$104,707³. As a percentage, this is equivalent to having invested the same money at a taxable rate of return of more than 16.24%⁴ compounded per annum for the 30 plus years of the investment!

When expressed as a tax paid real return (taking inflation out of the numbers) the rate is 4.24% compounded per annum for the 30 plus years. This is an excellent outcome as aside from forestry investment, what other investments have survived the last 30 years, beaten 7.54% average inflation, paid the tax due and still produced a similar positive return?

The confidence our pioneering Waterfalls Forest investors demonstrated in forestry investment and Forest Enterprises has been well rewarded.

S A R Wilton, Business Director
3 October 2002

¹ The All Groups CPI index has risen by a factor of 8.86 times from June 1973 to June 2002 therefore \$12,000 x 8.86 = \$106,300.

² A portion of the return is capital and therefore not taxed hence this figure is more than 55% of the taxable gross.

³ See footnote 2 above.

⁴ A 16.24% rate of return assumes a marginal tax rate during the period of 33 cents, whereas for most of the period the investors' marginal tax rates were probably more than 33 cents.