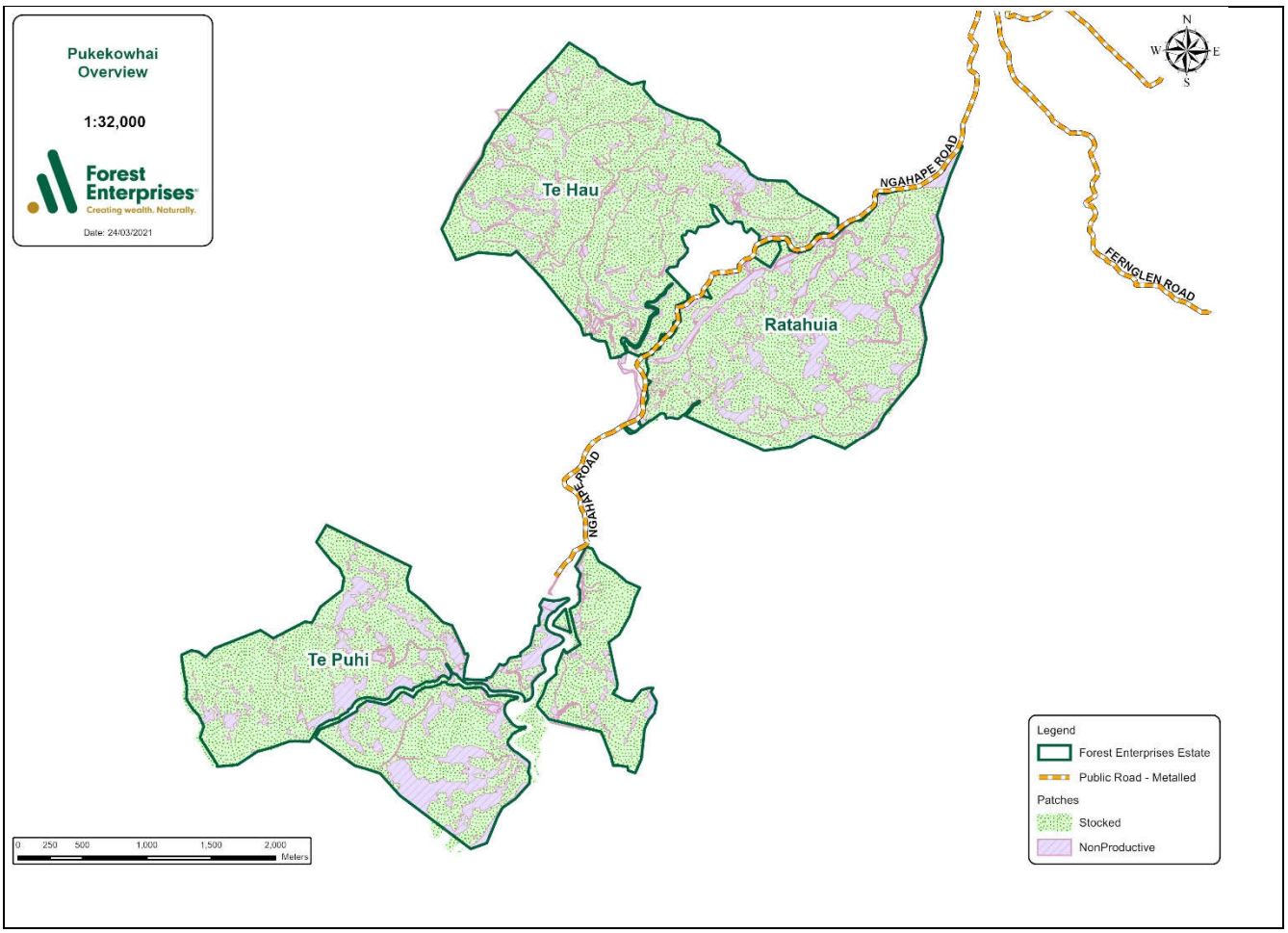
Overview of
Pukekōwhai Forest Proposal
and
Partner Exit Option

Overview of a proposal to combine the Ratahuia, Te Puhi and Te Hau Forests to maximise the return on the second rotation, and an option for those Partners (or their family) not wishing to participate in the second rotation.



Map of the Pukekōwhai Forest when fully established, showing the boundaries of the Participant Forests.

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IMPORTANT

The financial figures used in this Report were the best available figures when the document was prepared. If proceeding to a formal proposal is approved by the Participant Forests, the figures will then be finalised and this process may result in changes. These changes are not expected to be material, and will not impact the underlying principles and methodologies set out in this Report.

This Report is for information purposes only and is not a product disclosure statement or other offering document under New Zealand law. It does not constitute an invitation or offer of securities or financial products for subscription or purchase. If the proposal is approved for implementation, each Partner will then receive the statutorily prescribed information.

Introduction and Background

The Ratahuia, Te Hau and Te Puhi Forests (Participant Forests) are at various stages of harvest and subsequent replant of the second rotation.

The Participant Forests share three common objectives at this time –

1. To successfully and profitably complete their current harvest programs; and
2. To establish a second rotation forest which has the maximum profit potential for the next rotation; and
3. To provide an exit option at fair value for those Partners (or their family interests) who do not wish to continue for a second rotation.

Combining to form the Pukekōwhai Forest area creates the scale needed to maximise the return for the second rotation. Maximising the second rotation return is of benefit to both the second rotation Investors, and also to those Partners wishing to exit at the conclusion of the current harvest.

Executive Summary and Next Step

- **It is possible to create a combined forest from the Participant Forests of an estimated total net stocked area of around 800 hectares which maximises the profit potential for the second rotation.**
- **Partners wishing to exit will be able to do so on or before the end of the present harvest of their forest and release the value of their interest in the land and second rotation trees, whilst continuing to receive their share of the proceeds from the current harvest.**
- **Creation of the combined forest can be achieved at the same total cost which would be incurred were each forest sold separately post-harvest.**

It is intended that the combined forest be called the *Pukekōwhai Forest*. Pukekōwhai means ("Yellow Hill"), and is the peak behind Te Hau forest overlooking Te Hau, Te Puhi and Ratahuia Forests and the Ngahape Valley.

(The original name of Ngahape Group was used in early communications with Partners because it is the location of the forests. However, there are already other forests named 'Ngahape' including two managed by Forest Enterprises.)

Details of the Participant Forests

Refer to the separate maps on the cover of this Report and included in the presentation slides. Since 31 December 2020, further harvesting has continued in the Ratahuia and Te Puhi Forests.

Forest Area

The area details of the new combined investment are –

Forest Name	Gross Land Area	%	Projected Net Stocked Area	%
Ratahuia	302 hectares	29%	223.2 hectares	27.9%
Te Hau	346 hectares	33%	280.9 hectares	35.1%
Te Puhi	402 hectares	38%	293.4 hectares	36.7%
Johnsons Block	3 hectares	0%	2.5 hectares	0.3%
Total	**1,053 hectares**	**100%**	**800.0 hectares**	**100%**

Forest Enterprises has secured an additional 2.5 hectares (Johnsons Block) within the boundaries of Te Hau/Ratahuia, which will be added to the investment and provide better access given its location.

Second Rotation Treecrop

Area details of existing second rotation trees (Existing Hectares), plus the projected areas of second rotation trees still to be planted as harvesting continues (Projected Hectares), of the new Pukekōwhai Forest Investment are -

Forest Name	Existing Hectares	Projected Hectares	Total Hectares
Ratahuia	105.1	118.1	223.2
Te Hau	145.3	135.6	280.9
Te Puhi	25.3	268.1	293.4
Johnsons Block	2.5	0	2.5
Total	**278.2**	**521.8**	**800.0**

Existing hectares includes planting undertaken up to 2020.

Set-Up of Pukekōwhai Forest

Overview

1. Each Participant Forest partnership (Ratahuia, Te Puhi & Te Hau) will grant itself a forestry right over its remaining first rotation trees and continue its forestry business until the first rotation harvest is concluded, at which time the Participant Forest Partnership concludes.
2. Each Participant Forest Partnership–
   - 2.1. Will sell its land (subject to the newly created forestry right) to the Pukekōwhai Forest Investment for valuation. The current market value of each Participant Forest's land is being determined by the independent Land Valuer Mark Morice of Morice Limited.
   - 2.2. Will sell its existing second rotation trees for the value determined by the land valuer for trees planted in 2015 or earlier.
   - 2.3. Will sell its existing second rotation trees for the value determined on the basis of actual cost (bills paid), plus interest compounded at 2% per annum for trees planted after 2015. This is an established and approved methodology for calculating a fair value for young trees.

3. In return for the sale of the land and second rotation trees, each Participant Forest –
   3.1. Will receive an allocation of shares in the Pukekōwhai Forest equal to its proportionate share of the total land and second rotation tree value contributed by the Participant Forests.
   3.2. Will allocate these shares to their existing Partners.
4. Existing partners will have the option of subscribing for their allocation of shares or exiting and being paid for their share of land and replanted trees in their current partnership.
5. No Calls will be payable on Pukekōwhai Forest shares until June 2022, a date by which Partners in all Participant Forests wishing to exit have been able to do so. Details of the Exit Option are set out later in this Report.
6. The Pukekōwhai Forest will be set up as a Limited Partnership and registered as a Managed Investment Scheme under the Financial Markets Conduct Act 2013, the same investment structure used by Forest Enterprises for all new investments. How the structure works is available on request.

Further Detail on Some Key Set-Up Elements

Participant Forests Continue

Each Participant Forest Partnership will continue through until the conclusion of the present harvest and then wind up. Following the formation of the Pukekōwhai Forest, each Partnership will hold a Forestry Right securing ownership of the remaining trees (currently being harvested) plus any Pre-1990 carbon credits/New Zealand Units (NZUs). The NZUs were paid as compensation for loss of land value under the Emissions Trading Scheme for Pre-1990 Forest Area. [All NZUs relating to carbon lease arrangements of Post-1989 area have been received back from NZCL and have been sold.]

New Investment Pays for Second Rotation Planting from 2021

The new investment, not the Participant Forests, has responsibility to pay for replanting costs from 2021 onwards.

The cashflows underlying the proposal is based on the new Investment meeting all replanting costs from 2021 onwards.

The optimal time for the set-up of the Pukekōwhai Forest is in the first half of 2021. For this to occur, the second rotation trees contributed by each Participant Forest must be valued now.

Keeping it Simple is Paramount

The market valuation of the land has been assessed assuming the current harvest has been completed and the roading and associated infrastructure necessary to harvest the Participant Forests has been built. The difference in the productivity and profitability of each Participant Forest is reflected in their respective land values. The differences are not great because the forests adjoin or are in close proximity and located on land of similar quality for forestry purposes.

The value of the existing second rotation trees (Existing Hectares) has been calculated at actual cost plus 2% nominal interest compounded annually. The 2% rate is a net adjustment equivalent to a taxable interest rate of 3%. It could be argued that the interest rate should be higher or lower. Given that it is the same for all Participant Forests, the resulting value is consistently assessed for all forests.

No attempt has been made to use the harvest production actually achieved (or projected) this rotation. This is because production this rotation is a factor of site (taken into account by the land value), plus forestry factors such as quality of original tree stocks, climatic events (e.g. wind), silviculture regime (pruned and unpruned) and harvest age. In respect of most of these factors, the past is not necessarily a good indicator of the future.

The reality is that each of the three Participant Forests have combinations of similar and different characteristics, which have similar and different financial consequences on the Participant Forests and on the Pukekōwhai Forest Investment. The assumption is that, in combination, the pluses and minuses balance out, or if not the difference is immaterial.

Not ‘keeping it simple’ could potentially threaten the ability to implement this Proposal. Implementing the Proposal maximises the return for the second rotation which is of benefit to all the Partners of each Participant Forest. Achieving this overarching benefit must be remembered as a primary objective when reflecting on plus and minus consequences on individual Participant Forests.

Calls in Early Years to Fund Re-establishment of Pukekōwhai Forest

The initial cost for the for investment in Pukekōwhai Forest is primarily for land and any re-planting post-harvest of the Participant Forests up to 31 December 2020 (hence no initial cash cost for those investors opting to retain their shares). There is also the cost of acquiring the small Johnsons Block within existing forest boundaries and 2021 re-establishment which will initially be funded from borrowings.

The Pukekōwhai Forest is responsible for meeting the costs of re-establishment from 2021 onwards and paying annual Calls from 2022 onwards. Calls in future years will therefore mainly relate to the re-establishment of the remaining forest areas of around 522 hectares.

Calls only become payable to the Pukekōwhai Forest from the Partners who have elected to continue for the second rotation. Partners who choose the exit option will not pay any Calls to the Pukekōwhai Forest.

Partners will be able to put some of the remaining proceeds from their current investment aside to cover future costs if they opt to stay in the Pukekōwhai Forest Investment.

Value of Roading Networks within Participant Forests

The value of the harvest roading network being built by each Participant Forest passes to the Pukekōwhai Forest with the land. The valuation of the land includes the market value of the roads.

This methodology correctly ignores the actual investment per planted hectare of each Participant Forest. The actual cost reflects site specific factors and is the cost which must be incurred by the Participant Forests to be able to harvest the existing trees. Each Participant Forest is contributing a second rotation forest with the infrastructure needed to be able to harvest this forest. Any variation in the cost of this infrastructure per hectare consequently falls on the respective Participant Forest (is one of the pluses and minuses referred to earlier).

Rental Payable for Land in Use

If the Participant Forest Partnership is selling its land before the conclusion of the current harvest, it will be still occupying some of the land sold. This land use is addressed by each Participant Forest Partnership paying an annual land rental to the Pukekōwhai Forest for the actual area of land still in forest and still to be harvested. The land rental methodology was previously provided by the Land Valuer and it is proposed that it be based upon 4.75% of the value of the remaining 1st rotation stocked area per annum.

Implementation Cost

An important element of the viability of the proposal is ensuring that the implementation costs do not exceed the total cost which would be incurred were each forest sold separately. Selling separately would incur Real Estate commissions and legal costs.

Sale and Purchase agreements are required irrespective of whether each Participant Forest is sold separately, or to the Pukekōwhai Forest. The legal costs are therefore neutral.

Were each Participant Forest Partnership's land and second rotation trees sold separately, the cumulative standard Real Estate commissions and advertising costs could be 3-4%, which could be approximately $125,000. If the proposal proceeds, Forest Enterprises undertakes to complete the implementation at a fixed total cost of $75,000.

This fee includes the cost of Forest Enterprises' input into all the reports and documentation, calling and participating at Partner meetings, setting up the Limited Partnership, plus the cost of preparing the disclosure documentation, including a product disclosure statement, required under the FMC Act for an offer of financial products (the shares in the Pukekōwhai Forest Investment).

Contributed Value and Share Allocation

Total Value of Land and Trees Contributed by Participant Forests

The table below sets out the estimated total value of the land and trees contributed by each Participant Forest, and the resulting percentage contribution to the Pukekōwhai Forest.

Forest Name	Land Value	Existing Tree Value	Total Value	Percentage
Ratahuia Forest	$635,000	$316,000	$951,000	30%
Te Hau Forest	$956,000	$258,658	$1,214,658	39%
Te Puhi Forest	$939,000	$49,326	$988,326	31%
Totals	**$2,530,000**	**$623,984**	**$3,153,984**	**100%**

Share Allocation by Forest

Assuming there are a total of 80,000 shares in the Pukekōwhai Forest, the table below sets out the shares which will be allocated to each Participant Forest, based on the percentage contribution to the total value in the table above (these figures are estimates however any changes in the final workings are not expected to be material).

Forest Name	Percentage	Shares Allocated
Ratahuia Forest	30%	24,000
Te Hau Forest	39%	31,200
Te Puhi Forest	31%	24,800
Totals	**100%**	**80,000**

IMPORTANT

As highlighted on page 2, the figures in this Report are the best available when this Report was prepared. If a formal proposal proceeds, the figures will be finalised and any changes included. These changes are not expected to be material, and will not impact on the underlying principles and methodologies set out in this Report.

Exit Option Available to all Partners

Overview

The provision of an exit option at fair value, for those Partners (or their family interests) who do not wish to continue for the second rotation, is one of the key objectives of the proposal.

Implementation of this exit option will be achieved by Forest Enterprises contracting (guaranteeing) to purchase Pukekōwhai Forest shares from those Partners (or their family interests) not wishing to continue for the second rotation.

The formal mechanism will be partners assigning their proportionate interest in the Pukekōwhai Forest Investment to Forest Enterprises in exchange for payment. Those who choose to stay in Pukekōwhai Forest Investment will need to sign the application form included in the product disclosure statement (PDS).

The timing of being able to sign the application form or the assignment form will be later in the year once the PDS is registered.

Partners who wish to stay in the second rotation investment will be able to subscribe for additional shares or only take part of their allocation of shares. If there is existing Partner interest to subscribe for additional shares in 2021 over their allocation, these additional shares will be able to be subscribed for at a discount of 12.5% to the assessed value for the purpose of the Assignment, creating a benefit for an existing Partner buying (subscribing) for more shares than their entitlement.

Share Price Under the Assignment Option

Overview

The exiting Partner will receive their proportionate share of the value of the second rotation land and trees contributed to the Pukekōwhai Forest, less a discount. The discount is to compensate Forest Enterprises for providing this guaranteed exit at a fixed price, and for assuming all the resulting holding costs and sales risk (an Underwriting Fee). The Underwriting Fee will be 12.5%.

The quantum of the payment for the second rotation shares under the Assignment Option will be set out in a separate communication to Partners in each Participant Forest.

The Assignment Option Price per share in the Pukekōwhai Forest will be the same for Partners in each Participant Forest, as all partners will have the option to exit later in 2021.

Assignment Option Price in Context

The calculated value of the Pukekōwhai Forest shares, based upon the total value of the assets contributed (land and second rotation forest), is not necessarily the market value for the Pukekōwhai Forest. This would only be determined if the Pukekōwhai Forest was put up for sale.

There are currently few buyers in the market for young second rotation forests. The existing buyer interest is primarily for mid-rotation or older forests close to harvest. The offer value achieved from the market may be materially different to the market value used, and the offer value could be less.

The more relevant value comparison for each Partner is the market value of shares in each Participant Forest, as selling their interest in each Participant Forest is a Partner's alternative to not proceeding with the Pukekōwhai Forest Proposal. For the reasons expressed in this Report, this value is likely to be a materially lower amount than the assessed value for the Pukekōwhai Forest shares before the deduction of the Underwriting Fee.

Forest Enterprises will be on-selling the shares it purchases from Partners exiting under the Assignment Option. Our sales process will be supported by a material investment in marketing personnel and promotional campaigns, plus a second suite of disclosure documentation required under the FMC Act. Together with the cost of funding the share purchases, the total investment is expected to consume the 12.5% Underwriting Fee. We therefore plan to market the shares at the price before deduction of the Underwriting Fee.

Other Options to Consider

No Compulsion to Exercise the Assignment Option

There is no compulsion on Partners to exercise the Assignment Option. It is anticipated that many Partners (or family interests including family trust) will choose to continue for the second rotation. Partners are also able to transfer to other persons sourced by them at any time for whatever consideration they are able to negotiate.

Sell Some Shares Under the Assignment Option and Keep the Balance

An option some Partners may consider is to sell some of the shares and retain the balance. It is projected that the funds released from the sale of approximately 50% of the shares allocated in the Pukekōwhai Forest, if set aside, will be sufficient to meet the projected Calls through to 2029 (Calls do not commence until 2022). We can assist you with the calculation relevant to your shareholding.

Hold to Sell Some or All Shares via Forest Enterprises' Secondary Market

A Partner could also choose not to exercise the Assignment Option and instead plan to hold the shares at least until 2023. From 2023 it is expected that the Forest Enterprises secondary market will be available for the marketing of Pukekōwhai Forest shares by Partners. The reason the secondary market is not available before 2023 is discussed below.

Set Aside Some of the Current Harvest Proceeds for Future Calls

Some Partners may also choose to set aside some the proceeds from the current harvest underway, to be available in future to pay all or some of the Pukekōwhai Forest Calls from 2022.

Secondary Market Access Constraints During Initial Years

Forest Enterprises will be actively marketing the Pukekōwhai Forest shares purchased from Partners under the Assignment Option.

To ensure an orderly and efficient marketing process, Partners in the Participant Forests will not have access to Forest Enterprises secondary market to sell their Pukekōwhai Forest shares whilst the company is undertaking this marketing. Our marketing will conclude when the offer is fully subscribed and has closed, which is projected to be by the end of 2022.

As noted earlier in this Report, Partners are able to transfer to persons sourced by them at any time, be they family members, family trusts or third parties.

Financial Profile of the Pukekōwhai Forest

The projected financial profile of the Pukekōwhai Forest will be available when the formal proposal is voted upon early in 2021. The current draft indicates a competitive projected return for the Pukekōwhai Forest because of the benefits arising from second rotation.

The Pukekōwhai Forest will benefit materially as a result of –

1. being a second rotation forest; and
2. having a larger scale than each of the Ratahuia, Te Hau & Te Puhi forests; and
3. the unique benefits arising from the Pukekōwhai Grouping.

The benefits of being a second-rotation forest, of scale and of grouping, translate into increased Investor harvest proceeds as the expectation of yield will be 711 tonnes per hectare for the second rotation.

Based on current log prices at 31 March 2021, stumpage is predicted to be $37,958 per hectare.

Benefits as a Second Rotation Forest

Proven Ability to Produce and Sell a Radiata Crop

The Participant Forests have proven that –

1. a Radiata pine plantation forest can be successfully established and grown on the Pukekōwhai Forest land; and
2. it is possible to successfully harvest the forest and extract the logs produced to a public road; and
3. the regional distribution infrastructure exists to successfully transport the logs produced by truck, rail and ship to their ultimate customers.

Use of Existing Harvest Roading Network

By the completion of the current harvest, the Participant Forests will have built 35.2 kms of harvest roads and the associated landings plus other infrastructure. Although the substantial cost of this infrastructure is essentially a sunk cost to the Participant Forests, this infrastructure will materially reduce the roading and related costs for the second rotation harvest. Also, the improved accessibility from the roading network will considerably assist the management of the forest through to harvest.

Improved Forest Layout

Post-harvest the forest is being replanted consistent with how it was able to be harvested. This means that the second rotation crop will be of the same age in each harvest area. The age of the present crop when harvested is often mixed as it was planted to convenient boundaries (usually historical fence lines), with no regard to how and when it would be harvested.

Tree Stock Improvements

There have been significant genetic improvement in the tree stocks available today, compared with those planted in the 1990s. The genetic gains are known to produce more volume at the same age and also to produce the wood quality characteristics the market prefers.

Land Better Suited to Radiata Pine

The first rotation has changed the nature of the soil, and the fungi present, to best suit a Radiata pine tree crop. The second rotation crop will benefit from this improved soil environment.

Improved Management Knowledge

The ‘best practice’ management of a Radiata pine plantation forests continues to evolve over time. The second rotation forest will be managed in a manner consistent with latest ‘best practice’, and this will contribute further volume and quality gains to the second rotation.

Benefits Arising from Scale

Risk Mitigation

Adverse Event

The larger a forest, the greater the area available to absorb the consequences of adverse events, such as wind or fire. For example, the loss of 10 hectares in a 10 hectare forest represents total devastation, in a 250 hectare forest a material loss, but in a 600 plus hectare forest is relatively immaterial.

Market Exposure

The larger the forest (and the spread of age classes), the longer the time in the market at harvest. The longer the time in the market the greater the likelihood that the average log prices achieved will represent the long run average prices. Equally important, the longer the time in the market the less relevant the day-to-day log prices, especially the inevitable periods of low prices, as these are likely to be balanced by periods of high prices.

Cost Savings

Harvest Cost Savings

Harvest cost benefits arise when long term arrangements can be put in place with the harvesting service providers (harvest and cartage contractors etc). The long-term continuity of work for these service providers can remove from their prices the risk of down time from having to invest time securing future work. Also, harvest costs, such as the cost of resource consents and the cost of shifting equipment to the forest, are less of a financial burden the larger the forest.

Fixed Investment Cost Savings

The fixed investment related costs such as the financial and forestry audits, the supervisor fee, and financial markets compliance fees, are less of a financial burden the larger the investment. Even fees such as rates are proportionately less due to there being just one set of the fixed charge components.

Benefits Unique to the Pukekōwhai Forest

Contiguous Forest Areas

The contiguous forest area of Ratahuia and Te Hau forest properties and the close proximity of Te Puhi in the Pukekōwhai Forest further enhances the Harvest Cost Savings identified above.

Interconnected Harvest Roads

The contiguous forest area within the Pukekōwhai Forest also means that much of the roading network is interconnected. Branches of the Te Hau and Ratahuia networks are interconnecting roads.

Complimentary Age Classes

The complimentary age classes of the Participant Forests translate into a 10-year harvest profile which enhances the benefit of Market Exposure Risk Mitigation identified earlier. It is also appealing to Investors looking for a revenue stream over a longer period.