

9 November 2012

The Manager  
Company Announcements  
Australian Stock Exchange Ltd  
4<sup>th</sup> Floor, 20 Bridge Street  
SYDNEY NSW 2000

Dear Sir/Madam

**RuralAus Investments Limited ("RuralAus")**  
**ACN 091 247 166**  
**Meetings of Growers – Possible termination of Projects**

The directors of RuralAus wish to announce to shareholders that Primary Securities Limited ("Primary Securities") have called a Meeting of Growers for the following Projects:

- Plantation Forestry Hardwood Project No1;
- Plantation Forestry Hardwood Project No 2;
- Australian Growth Timber Project No 3;
- Australian Growth Timber Project No 4; and
- Australian Growth Timber Project 2002/2003.

Primary Securities is the responsible entity for the above Projects.

The purpose of the Meeting is to discuss the possible winding up of the Projects. Accompanying this letter, are copies of the Notice of Meeting, an Explanatory Statement from Primary Securities to the growers, a letter from RuralAus to Primary Securities about the financial implications to RuralAus and a copy of the Viability Report as prepared by RuralAus Plantation Management Pty Ltd ("RAPM").

Shareholders should be aware that RAPM, a subsidiary of RuralAus, has in its role as plantation manager been conducting a marketing campaign over the past 12 months, to try to realise commercial value from the sale of the woodchips from harvest of the various Projects. This has not resulted in any purchasers of the woodchips, but has confirmed a very steep decline in the woodchip export price caused by a number of external factors, as detailed in RuralAus' 2012 Annual Report.

The results of this marketing campaign led to RAPM completing a viability study of all of the Projects, with the findings being that at the current and forecast woodchip export price for the next several years, the Projects are unviable. RAPM has further concluded that the return to growers after taking into consideration the costs of harvest would be less than the lease and management fees payable from this point on until harvest. The Independent Forester appointed by Primary Securities has also confirmed this conclusion.

The winding up of the Projects has material implications for RuralAus.

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If the Projects are wound up, RuralAus will not receive any further lease and management fee income, nor would it receive interest income. Regarding Project 1, as these loans are non-recourse, the principal to growers would also be forgiven pursuant to the terms of the loan agreement.

As the landowner on Kangaroo Island, RuralAus will assume ownership of the trees and responsibility of all ongoing costs associated with those Projects. However, currently all plantation trees on Kangaroo Island are valueless. For any return on these trees, considerable infrastructure investment would be required. Even with a considerable improvement in all markets, there is still no guarantee of a positive economic return in the short/medium term.

In relation to Bremer Bay, as the head lessee, provided RuralAus continued to make lease payments to the landowners, RuralAus would maintain the rights to the timber on those properties. However, initial studies indicate that the return from the Bremer Bay properties would be insufficient to meet the ongoing lease payments and eventual harvest costs from those plantations, and therefore it is likely that RuralAus will not continue to make the lease payments for the Bremer Bay properties.

RuralAus will continue to explore all available commercialisation options at the Parndana Timber Mill. Whilst the mill is not yet contributing an operating profit to RuralAus, the Board and Management plan to materially increase operations at the mill by commencing use of the treatment plant, kilns and dry mill to produce higher margin products.

In addition, RuralAus is applying for further Federal Government funding to continue the study into the biomass power plant on Kangaroo Island, as the board firmly believes that there is genuine need for an alternative source of renewable electricity generated on the Island.

The above is likely to result in structural changes to RuralAus, however, these changes have not yet been finalised. It will also highlight a short/medium term need for additional funding to bring the board's strategies for the mill and renewable power to fruition and therefore a capital raising is likely in the near future.

RuralAus wishes to highlight to Shareholders the change in focus from production and sale of woodchips to other plantation timber products, necessitated by external market forces.

Should shareholders wish to discuss the above, please contact Paul McKenzie (Chairman), John Ipsen (Chief Executive Officer) or myself.

Yours faithfully



Scott Wallace  
Company Secretary  
RuralAus Investments Limited

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## PRIMARY SECURITIES LTD

6 November 2012

Dear Grower

**Plantation Forestry Hardwood Project ARSN 115 525 196**  
**Plantation Forestry Hardwood Project No 2 ARSN 087 818 782**  
**Australian Growth Timber Project No 3 ARSN 093 113 565**  
**Australian Growth Timber Project No 4 ARSN 096 164 153**  
**Australian Growth Timber Project 2002/2003 ARSN 100 466 126**

### 1. Viability

Downward pressure on woodchip prices has continued since RuralAus reported to you in an "Update from the Chief Executive Officer, 30 May 2012".

Today, we consider most blue gum plantations in Australia to be unviable or at best marginally viable.

The continuing high value of the Australian dollar versus the US dollar is the cause of what we refer to as negative stumpage. Negative stumpage means Growers would have to pay more to have their trees harvested and transported to a shipping port than they would receive in sales proceeds.

Attached to this letter is a "Viability Report" prepared by RuralAus Plantation Management Pty Ltd (RuralAus), the Schemes' manager. The report concludes that all Schemes are not viable.

We must now consider early termination of all Schemes.

A meeting to discuss whether Growers should terminate or continue will be held on 29 November 2012. A notice of meeting is attached.

We agree with the findings of the report.

### 2. Major Factors affecting Viability

#### 1) **Price for Woodchips**

Buyers are offering US\$150 or less. This translates to A\$145 (at an exchange rate of US\$1.03 per A\$1.00).

In earlier times US\$150 would have translated to A\$200 (at an exchange rate of US\$0.75 per A\$1.00)

The Schemes are viable at an exchange rate of US\$0.75.

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## 2) **Terms of Leases**

All leases are near to (within a few years of) their expiry date. Growers are obliged to vacate their woodlots on expiry, whether their timber has been harvested or not. They give up all rights to their timber on expiry.

The terms of the leases may be extended further but we do not believe that the cost would be justified. (See Section 4).

## 3) **Forward Exchange Rates.**

We have discussed forward exchange rates with two of the major banks. The outlook for the next 12 months is not for a fall against the US Dollar. Demand for the A\$ remains very strong from major countries where the interest rate for deposits sits at around 0.

### 3. **RuralAus Financial Modelling**

We have thoroughly reviewed and tested the financial model(s) used by RuralAus and are comfortable with the underlying assumptions relating to yields, prices, costs and fibre/moisture content.

#### (a) **Yields**

Yields vary marginally from Scheme to Scheme but are consistent with the independent forester David Geddes Analysis of between 70 and 100 cubic metres per hectare.

#### (b) **Prices**

RuralAus used the current industry offer rate of \$145 for Scheme 1 and higher rates, \$165 to \$170 for Schemes 2 to 5 in anticipation of an uplift in prices in the near term. We can find no justification for modeling a higher price and the outlook could in fact be worse than the RuralAus' forecasts.

#### (c) **Costs**

Our forester has reviewed costs of harvesting, transport, handling etc and found these to be reasonable (even on the low side).

#### (d) **Moisture Content**

RuralAus have adopted a conservative percentage. Actual dry fibre yields may be marginally higher but not sufficiently to have any real impact on the model.

**4. Projected Returns per Woodlot**  
**(Assumes no Returns from Kangaroo Island Plantations)**

Project	Price per BDMT	<u>Projected Returns Today</u>		Returns at \$207 BDMT (before fees)	Lease Expiry Date
		Before Fees	Fees Included		
1	\$145	\$(348.36)	\$(598.36)	\$4872	BB 30/6/2013
2 (a)	\$165	\$232.33	\$(17.61)	\$1,419	BB 30/6/2014 KI 29/6/2014
(b)		\$23.33	\$(344.22)		
3 2000 2001	\$165	\$95.01	\$(769.81)	\$870	BB 30/6/2013 KI 29/6/2014
		\$95.01	\$(720.85)		
4 (a)	\$165	\$(217.13)	\$(217.13)	\$1,035	BB 30/6/2013 KI 29/6/2014
5 (a)	\$165	\$(96.84)	\$(96.84)	\$384	BB 30/6/2014 KI 29/6/2014

Note: Returns to All Growers are impacted by a forecast nil return from the Kangaroo Island Plantations, meaning all Growers in each scheme share only in proceeds from Bremer Bay.

Independent foresters Poyry Forestry Industry Pty Ltd issued Reports in June 2009 recommending early termination of Schemes 4b, 4c, 5b and 5c as they were considered not commercially viable. Growers voting at a general meeting convened in April 2010 voted to continue those Schemes. These Schemes are all located on Kangaroo Island. Details of these Schemes are;

4b	Nitens	183 Ha
4c	Pine	163 Ha
5b	Nitens	139 Ha
5c	Pine	18 Ha
5c	Nitens	77 Ha

**5. Kangaroo Island**

In addition to those Schemes mentioned above, Schemes 2, 3 and 4 all have plantations on Kangaroo Island. RuralAus does not believe that there is any possibility of economically harvesting and transporting logs to the mainland.

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These plantations were always dependent for their viability on the construction of a port. The likelihood of a port being constructed in the near future remains remote, particularly in view of the low prices currently being offered for woodchips and logs. A port cannot be constructed prior to the expiry of leases.

The owner of the land at Kangaroo Island is RuralAus. They may ultimately benefit from ownership of the trees.

## 6. RuralAus Financial Results

RuralAus is the subsidiary of a listed public company, RuralAus Investments Limited, which has reported a net loss for the year ended 30 June 2012 of \$3.942 million in its audited financial statements.

RuralAus Investments Limited reported as follows:

"A substantial increase in the allowance for impairment on the outstanding grower loans of \$3.373m (2011: \$1.794m) was expensed in the accounts during the year and was the single largest contributing factor to the loss reported by the group this year. This expense was a result of a review of the grower loans and relates to the expected forecast return that may be paid to growers on harvest. This expected return directly affects the recoverable amount of the loans. The reason for the increase is a substantial fall in the woodchip export price from the previous four-year's price of \$207.40/bone dry metric tonne ("BDMT") to the current level of approximately \$150/BDMT."

RuralAus Investments Limited stands to lose \$6.9m in the winding up of the Schemes. We refer Growers to the attached letter from the CEO of RuralAus Investments Limited.

Growers will be aware of substantial write downs in the value of plantations, the most significant being Gunn's writedown in excess of \$1 billion which ultimately led to Gunn's demise.

## 7. Unpaid Lease and Management Fees

Lease and management fees for all Schemes were invoiced during June 2012. As at the date of this report, the position in regards outstanding fees can be summarized as follows:

	<u>Lease fees</u>	<u>Management fees</u>	<u>Total</u>
Outstanding at May 2012	164,422	171,696	336,118
Invoiced during June	337,978	623,038	961,016
Collected to 30 September 2012	(181,001)	(391,668)	(572,669)
Outstanding as at 30 September 2012	321,339	403,066	724,465

The level of outstanding fees is significant and reflects the reluctance of many Growers to continue supporting these Schemes.

## 8. Outstanding Loans

Growers in Scheme 1 with outstanding loans will have those loans forgiven if the Schemes are wound up with no requirement to repay the outstanding principal, pursuant to their loan agreements.

Growers with original loans in Schemes 2 to 5 would be required to immediately pay any outstanding balance, however we understand that this effects only four borrowers.

## 9. What Happens on Termination

If Growers resolve to terminate the Scheme, they cease to have any participation in the Scheme and have no further liabilities or entitlements to revenue from the trees. RuralAus as the head-lessor becomes entitled to the leases and trees in so far as they wish to maintain their head leases. It should be noted however, that no RuralAus company owns the plantation land at Bremer Bay,

## 10. Conclusion

The strong Australian dollar is likely to continue. Woodchip prices will remain depressed for some time.

Growers' leases will expire in the near future. Growers do not have the opportunity to wait for a turnaround in the current economic cycle.

We recommend that the Schemes be terminated.

RuralAus have given us an undertaking that they will repay half of the lease and management fees invoices received for 2012/13. Those Growers that have not yet paid these lease and management fees will be requested to do so, failing which, it is likely that RuralAus will take action to recover this amount.

Yours faithfully  
**PRIMARY SECURITIES LTD**



Tony Treadgold  
Chairman

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## PRIMARY SECURITIES LTD

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NOTICE is hereby given that concurrent Meetings of Members of the following schemes will be held at 2.30 pm on Thursday, 29th November 2012 at the Cottesloe Beach Hotel, 104 Marine Parade, Cottesloe, Western Australia:

Plantation Forestry Hardwood Project ARSN 115 525 196

Plantation Forestry Hardwood Project No 2 ARSN 087 818 782

Australian Growth Timber Project No 3 ARSN 093 113 565

Australian Growth Timber Project No 4 ARSN 096 164 153

Australian Growth Timber Project 2002/2003 ARSN 100 466 126

### **BUSINESS**

To discuss the viability and possible early termination of the five schemes.

### **By order of Primary Securities Ltd as Responsible Entity**

Robert Garton Smith  
Managing Director

Date: 6<sup>th</sup> November 2012

### **Notes**

- a. If you are unable to attend the meeting you may send a representative to attend in your place. No proxy form is necessary.
- b. Please see the attached Explanatory Memorandum giving the reasons for the meeting.

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# EXPLANATORY MEMORANDUM

## REASONS FOR MEETING

### Schemes not considered viable

Documents attached to this notice of meeting, are:

- a Viability Report of the Bremer Bay MIS Plantation Estate Schemes, with commentary on the Kangaroo Island Schemes prepared by the manager, RuralAus Plantation Management Pty Ltd (**RuralAus**); and
- a letter from Primary Securities Ltd (**Primary**) regarding the Viability Report.
- A letter from RuralAus Investments Limited advising of the "Financial Impact on RuralAus on Termination of Schemes".

Please read these documents

In summary, RuralAus has concluded that the Schemes are not viable. We agree with this conclusion.

If the Schemes are not viable then Growers should not pay further rent and management fees and the Schemes should be terminated.

### RuralAus proposal

RuralAus proposes that all of the Schemes be terminated.

If this happens, in the case of Growers who have paid their fees for the current financial year, RuralAus will refund one half of the fees.

In the case of Growers who have not paid their fees for the current financial year, RuralAus will give Growers a credit note for half the fees but the balance remains owing. [Note that for some of the Schemes, no annual fees are payable]

Outstanding loans will become payable if any Scheme is terminated, but we understand that this affects only four Growers.

### Purpose of the Meeting

The purpose of the meeting is to

- discuss the Viability Report
- enable Growers to ask RuralAus and Primary any questions they may wish to ask regarding the viability of the Schemes.

At the end of the meeting(s), a straw poll (non-binding vote by Growers) will be taken on a show of hands as to whether or not the Schemes should be terminated.

### Notice of proposal to wind up the Scheme

Depending upon the results of the meeting, Primary may give Growers notice that it proposes to wind up some or all of the Schemes on the grounds that the purpose of the Scheme cannot be accomplished (a notice under section 601NC(2) of the Corporations Act 2001).

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Growers who do not want their Scheme wound up will have the right to take action (under Division 1 of Part 2G.4) to call a Growers' meeting to consider the proposed winding up of the Scheme and to vote on any extraordinary resolution Growers may propose about the winding up of the Scheme. To call such a meeting requires the support of 5% of the Growers. Those Growers would be required to pay the costs of the meeting.

If Growers do not call a meeting to consider the proposed winding up (or continuation) of the Scheme within 28 days of being given notice by Primary, then Primary will be permitted to wind up the Scheme.

### **This meeting avoids cost for Growers**

Rather than simply issue a notice that the purpose of the Scheme cannot be accomplished, and then put the onus on Growers to call a meeting at their cost, Primary would rather call the meeting (at the cost of RuralAus) and give Growers an opportunity to be involved in the decision as to whether the Scheme(s) should be terminated.

### **Final termination process**

If Primary proceeds after the meeting to give notice that it proposes to wind up the Scheme, then the 28 day period will expire in the last few days of December. The Scheme agreements will be terminated as at the end of December 2012 on condition that RuralAus refund half of any fees paid during the year. Primary will assign to RuralAus the right to collect unpaid fees.

ASIC will then be asked to deregister the Scheme. This process takes some months.

### **What is the effect of termination?**

Growers lose all rights.

### **If Growers want their Scheme to continue**

Growers in Schemes which require payment of rent and management fees will have to continue to pay these.

### **What does Primary recommend?**

Unless there is evidence to the contrary forthcoming, Primary recommends that the Schemes be terminated.

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# **RuralAus Plantation Management Pty Ltd**

ABN: 24 114 145 498

**Viability Report of Kangaroo Island and Bremer Bay MIS Plantation Estate Projects**

As at 2 November 2012

### Important disclaimer

The viability modelling of the standing and forecast wood volumes presented in this Report is based on publicly available pricing documentation as well as personal communications with woodchip and other buyers.

It should be recognized that a number of international factors such as exchange rates, shipping rates and general Asian Pacific supply and demand factors will have an influence on the sales price between this point in time and time of harvest. The Report as prepared must be considered taking this into account.

### Preamble

RuralAus Investments Limited ("RuralAus") understands that growers entered into a number of Projects between 1998 and 2002 developed, marketed and managed by Australian Growth Limited ("Australian Growth"). A number of assumptions of productivity and price were included in the various prospectuses offered to the market. These were long-term forecasts and estimates of an industry in its infancy.

Growers invested in these Projects in good faith based on a combination of taxation incentives and estimated returns.

Whilst growth in a number of Projects has been below forecast at Bremer Bay, Kangaroo Island has been performing at or above forecasts on much more productive land.

Since the Projects were established, the Australian benchmark woodchip price has progressively increased, as have sales volumes into Japan. This culminated in record tonnages at a price of AUD207.40 for plantation woodchips during 2010 and 2011. As considered in this Report a number of factors have led to a decline in volume and a significant decrease in price during 2012.

The Managed Investment Scheme ("MIS") industry increased significantly during the period 1999 to 2008 and fell spectacularly with the demise of the main industry players in 2009 and 2010.

As a result of the rapid pace and scale of MIS investments, over one million hectares of plantations have been established across Australia creating significant investment and employment in rural and regional areas.

Australian Growth was not without its own financial difficulties, being placed into Voluntary Administration in 2003 and subsequently recapitalised as RuralAus in May 2005, with new management and directors. At that time, the Responsible Entity, Australian Growth Managers Limited, was sold out of the Group to Primary Securities Limited, who has held the position of Responsible Entity since that date.

Since that time, RuralAus has been managing these Projects in the best interests of the growers and has at all times sought to provide maximum returns to growers.

As was advised to growers in 2005, RuralAus invested \$2.0m of its own shareholder funds to continue with the various Projects and has invested a further \$700,000 since that date through enhancing plantation growth by broad scale fertilising, replanting where required and bringing the plantations up to a generally accepted industry standard.

The attached Report provides RuralAus' view of the current status of the various Projects.

## Executive summary

This Report concludes that all of the Projects be deemed unviable and RuralAus therefore recommends to the Responsible Entity that all Projects be wound up.

The viability modelling of the Kangaroo Island and Bremer Bay MIS plantation estate draws on the data provided in the accompanying Standing and Forecast Volume Report provided by RuralAus Plantation Managers (RAPM).

We have forecast returns to growers in each Project per woodlot after taking into account projected harvest income, harvest costs and costs to growers by way of outstanding lease and management payments that would be deducted at the time of harvest. The forecast returns are negative for all projects.

## 1 Introduction

RuralAus undertook a remeasure of the permanent sample plots located throughout the *Eucalyptus globulus*, *Eucalyptus nitens* and *Pinus radiata* MIS estate under management. To improve the accuracy and precision of the measurements a significant number of additional plots were added where it was deemed additional measurements were required to reflect site variability and changing soil type. The measurements commenced late 2011 and were concluded early September 2012.

This Report uses the data generated to provide a range of estimated standing timber values based on a net present value.

The Report builds on information provided to growers over the past twelve months.

## 2 Background data

### 2.1 Terminology

The following table of terms is used in this document:

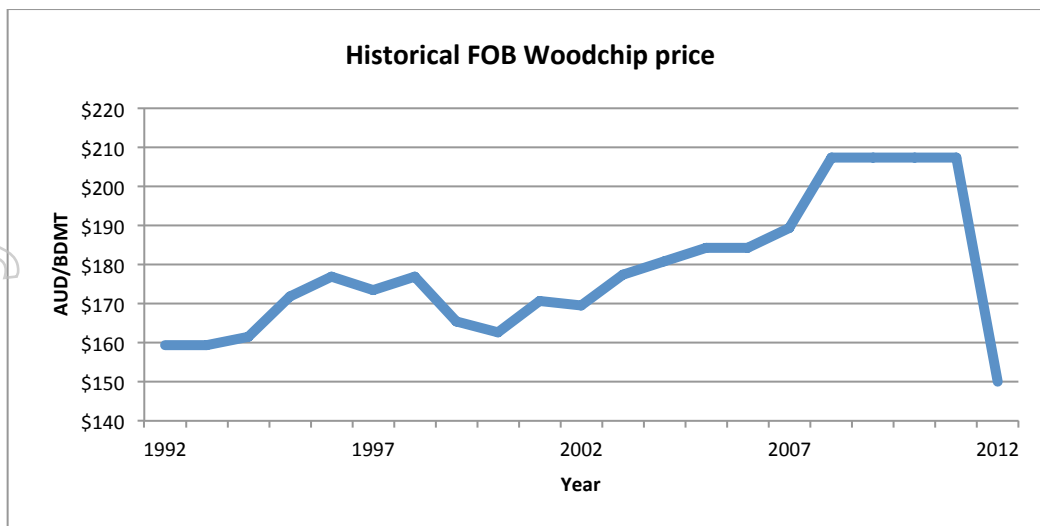
GMT	Green metric tonne – (= 1 cubic metre of standing timber)
BDMT	Bone dry metric tonne – (the quantity of fibre in one kg of dry fibre – approximately 2 GMT – 1 BDMT)
FOB	Free on board at loading port – (woodchips loaded into a ship)

### 2.2 Long term historical sales prices

Prior to 2012 woodchip sales were generally sold under long-term sale contracts to Japanese pulp and paper companies, usually in conjunction with a Japanese trading house. Sales were by way of a “benchmark” woodchip sales price negotiated annually by the major woodchip purchasers. This then became the standard for all woodchip buyers.

The GFC impact, the Japanese Tsunami, the significant rise in the Australian dollar and the financial stress suffered by a number of major Australian forest growers have lead to a breakdown of this long-term sales structure. The emergence of China as an increasing woodchip buyer has also lead to downward pressure on prices. The reasons for this is that the Japanese pulp mills were willing to pay premium prices for higher quality Australian woodchips and for long term supply certainty whereas the Chinese pulp mills prefer to maximise short term profit by using cheaper, lower quality woodchips on shorter term contracts. Accordingly, the Japanese pulp mills are finding it increasingly difficult to compete with the Chinese pulp mills and are therefore buying less woodchips.

Below are the historical plantation hardwood woodchip prices since 1992 to 2011 as obtained by RuralAus



**Graph 1 Historical woodchip prices**

We are aware that woodchip sellers have been receiving a range of discounted prices to that of the 2011 benchmark price, sales to China are significantly below this. Without any firm Japanese price offers the best price that has been received by RuralAus to date has been AUD145/BDMT into China. We have used this price for our 2013 starting assumption.

### 2.3 Previous grower updates

A Woodchip market update was provided to Project 2 – 5 growers as background and supporting documentation in May 2012.

These referred to a number of public statements by forest growers in their market updates:

- Gunns Limited ASX Market Update announcement – December 2011
- Great Southern Plantations (GSP) Quarterly grower update March 2012
- Elders Forestry Market Update – March 2012

Subsequent to these announcements, a number of materially adverse events have occurred:

- Elders Forestry ASX Announcement – 16 April 2012. Elders advised that a number of forestry land and pulpwood assets had been sold to Global Forest Partners (GFP). Under the transaction GFP have offered to purchase some of the standing timber held by investors in a number of pulpwood projects managed by Elders Forestry. The Supreme Court of Victoria confirmed on 16 May 2012 that Elders Forestry, as RE, can sell the standing timber as prescribed. Elders considered that **“current and foreseeable market conditions for woodchips are extremely poor and the marketing of woodchips has moved to “spot sales” with the dismantling of the annual off take negotiations which previously applied. This has been caused by a number of factors ..... including the following:**
  - Appreciation of the Australian dollar
  - Reduced Japanese demand
  - Increasing SE Asian woodchip supply
  - Australian “supply overhang” exacerbated by delayed harvest
- Gunns Limited ASX Market update – 6 August 2012. This stated that: **“Woodchip markets have continued to decline over the course of the past 3 months with both the selling price and sales volumes under considerable pressure. The Company does not expect these conditions to improve in the near to medium term, due to the significant and growing oversupply of plantation woodchips available from Australia and an expectation that the Australian dollar will remain around current levels compared to the US dollar”.**
- Gunns Limited appointed a Voluntary Administrator on 25 September 2012 and subsequent Receivership on 26 September 2012.

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### 3 Forecast harvest volumes

The following table is taken from the Inventory Report attached to this Report and provides an estimate of standing volume per Project at harvest time.

Location	Project No	Species	Planted Area (Ha)	Volume Available at Harvest (m3)
BB	1	E.globulus	1,221.2	100,805
BB	2	E.globulus	1,290.0	109,724
BB	3	E.globulus	136.7	8,559
BB	4	E.globulus	198.2	14,206
BB	5A	E.globulus	100.1	7,942
			2,946.3	241,236
KI	2A	E.glob/nitens	132.5	38,344
KI	2B	E.globulus	562.0	174,265
KI	3	E.globulus	103.0	32,114
KI	4A	E.globulus	34.0	12,548
KI	5A	E.globulus	166.0	66,802
			997.5	324,073

**Table 1 Summary of forecast volumes**

As has been highlighted on a number of occasions over recent times, the plantation productivity at Bremer Bay is generally considered to be very low as a result of a number of years of drought following initial planting. Growth and hence timber volumes at Kangaroo Island are considerably better than Bremer Bay.

### 4 Harvest plans

The indicative harvest schedule shown in Table 2 assumes a production rate of 80,000m<sup>3</sup> of plantation to be harvested per year with harvest operations commencing in 2013 for Project 1 in Bremer Bay.

The indicative timings are based on the expiry dates for each Project (as indicated in the Prospectus and as agreed by extension). The table provides a forecast of standing volume forward from the current inventory estimates.

Project No	Harvest Volume	Year of Harvest	2013	2014	2015	2016
1	100,805	2013	80,000	20,805		
2	112,198	2014		59,195	53,003	
3	9,287	2015			9,287	
4A	14,977	2015			14,977	
5A	8,369	2016				8,369
	245,636		80,000	80,000	77,267	8,369
Forecast FOB price			145	165	165	170
Harvest Cost			76.00	78.28	80.63	83.05

**Table 2 Harvest schedule based on Project expiry dates.**

## 5 Sales assumptions

### 5.1 Bremer Bay

RuralAus has spent the last 12 months attempting to market the Bremer Bay woodchips for sale to various Asian trading houses, including a trip to Japan and Singapore, numerous trips to Korea and many discussions with various woodchips purchasers in Japan.

A number of Japanese trading houses have shown interest in marketing woodchips for sale on a spot shipment basis into the Chinese and Japanese market, however, the prices that are being offered to RuralAus are considerably lower than the traditional woodchip export price of the last four years (refer Section 2.2 above).

The effects of the GFC, Japanese tsunami, high Australian dollar and the closure/failure of a number of woodchip exporters in Australia have seen a dramatic reduction in the woodchip export price from Australia.

Unfortunately the relatively small volumes of timber that RuralAus would be able to export for growers has meant that RuralAus is a "price taker" in the market, as we don't have sufficient scale to demand higher prices.

The best price that has been offered to RuralAus as at the date of this Report is AUD145/BDMT.

In relation to the harvest costs, RuralAus has held many discussions with potential harvest operators and have secured harvest and haulage operators who are able to commence harvest at Bremer Bay when required. The best price that we have been able to negotiate has been AUD76/GMT. The relatively poor tree growth (resulting in higher harvest costs) and distance to port (170km+) are the main contributing factors to this cost.

The income figure of AUD145/BDMT and the cost figure of AUD76/GMT have been used in calculating the initial returns to growers. We have used various expert reports in relation to forecasting the woodchip export price for periods beyond 2013 and have escalated harvest costs by 3% per annum.

The following table summarises the assumptions used in assessing timber at Bremer Bay:

	March 2011	October 2012	2014/15	2016
FOB price AUD/BDMT	\$207.40	\$145.00	\$165.00	\$170.00
Percentage dry fibre	52%	52%	52%	52%
Conversion to FOB AUD/green tonne	\$107.85	\$75.40	\$85.80	\$88.40
Operating costs/green tonne	\$76.00	\$76.00	\$78.28 - \$80.63	\$83.05
Gross stumpage	\$31.85	(\$0.60)	\$7.52 - \$5.17	\$5.35

See Section 6, Projected returns to Growers.

### 5.2 Kangaroo Island

As stated in earlier advice to growers, we considered that it was unlikely that a Woodchip Export Terminal would be constructed on Kangaroo Island. This has become even less likely with the announcement that Gunns Limited, the Responsible Entity and market purchaser of the Great Southern estate on Kangaroo Island, has gone into receivership owing \$500million to its banks, casting further doubt on the future of the timber resources on the island.

We had highlighted other possible scenarios for the timber on Kangaroo Island, which are discussed below.

#### 5.2.1 Biomass power station

RuralAus received a grant from the Government of South Australia in 2011 to conduct a feasibility study into the construction of a biomass power plant on Kangaroo Island for use at the Parndana Timber Mill and with surplus power to be supplied into the general electricity grid. The results of this study were positive, with RuralAus now applying for an additional Federal Government grant to further this study.

Whilst we expect the results of the further study to also be positive, the fact remains that this project is very uncertain. There are numerous factors that need to be overcome, including many levels of government approval and the main issue, being the connection into the electricity grid, which will require a substantial



upgrade of the electricity infrastructure on the island. It is for this reason that the plant may never actually be constructed.

Given this inherent uncertainty, we cannot guarantee that the growers' timber on Kangaroo Island will be used in a biomass power plant.

## 5.2.2 Log exports

RuralAus has been trying for a number of years now to commence the export of logs off Kangaroo Island, however, the log export price, like the woodchip export price, has been depressed for a number of years. This has resulted in the cost of export exceeding the income, making log exports financially unviable. Based on our industry knowledge, unfortunately, we do not see this position reversing any time soon in the future.

Accordingly, we do not believe that this is a viable alternative for the growers' timber on Kangaroo Island.

## 5.2.3 Processing of timber at Parndana Sawmill

You will be aware that RuralAus purchased the only operational sawmill on Kangaroo Island in 2010. One of the objectives of the purchase was for the possible processing of growers' timber on the island. Despite our best efforts, the financial viability of the timber mill remains uncertain. We are presently processing RuralAus owned timber through the mill, which while producing excellent sawn product, from a financial perspective, the sawmill is running at a loss.

This loss is with RuralAus paying no stumpage fees for its owned timber, meaning that even with the trees being free to RuralAus, the sawmill has still been unable to make money.

Given the financial situation with the mill, its future beyond December 2012 remains uncertain and therefore the use of growers' timber through the sawmill is unlikely to ever occur.

## 5.2.4 Conclusion on Kangaroo Island sales assumptions

Given the above points, we are of the opinion that none of the growers' timber will be able to be exported from Kangaroo Island and therefore we consider that this timber is valueless. Accordingly, in calculating the possible return to growers, we have assumed that there will be no return for timber on Kangaroo Island.

# 6 Projected returns to growers by Project

Detailed Project modelling is provided in Appendix one attached.

## 6.1 Net stumpage derivation

AUD Woodchip price per BDMT	\$145/BDMT
Conversion to GMT (@48% moisture)	52%
AUD per GMT	\$75.40
Harvesting and marketing Costs per GMT	
Stockpile losses	\$1.00
Port Handling	\$16.50
Road Haulage (170km to Port)	\$19.00
Harvesting (80 – 100 tonne/ha)	\$38.00
Roading costs	\$0.50
Harvest Supervision	\$1.00
Total Costs	(\$76.00)
<b>Net Margin (AUD per GMT)</b>	<b>(\$0.60)</b>

## 6.2 Project 1

Project 1 can be summarised as follows:

Location of plantation/s	Entirely at Bremer Bay
Total number of woodlots	610
Total projected volume of timber	100,805 GMT at Bremer Bay
Woodchip export price	AUD145/BDMT
Moisture content	48%
Harvest schedule	January 2013 to June 2014
Harvest costs	AUD76/GMT
Lease and management fee charged	\$250 pa (non indexed)
Years of lease and management fees to pay until harvest	1 further year
Projected return per woodlot (before L&M fees)	(\$348.36)
Projected return per grower (after taking into account L&M fees to be paid)	(\$598.36)

As can be seen above, the projected return to growers is negative \$348.36 per woodlot, before even taking into account the lease and management fees to be paid on the remaining year of the Project, as the costs to harvest exceed the gross harvest income. At a FOB price of AUD150/BDMT, the return to growers would still be negative, as the income per woodlot would be insufficient to cover the final year's lease and management fees. Accordingly, we consider that this Project is unviable and should be ended as soon as possible.

## 6.3 Project 2

Project 2 comprises two types of projects: Part A, comprising 1999-2a and 2000-2a and Part B, comprising 2000-2b. Growers in each part of the Project pay differing rates of lease and management fees, however all share in the same pooled harvest income. Project 2 can be summarised as follows:

Location of plantation/s	1,262 ha at Bremer Bay, 704 ha at Kangaroo Island
Total number of woodlots	1,966 – 2a comprising 926 woodlots, 2b comprising 1,040 woodlots
Total projected volume of timber	109,724 GMT at Bremer Bay
Woodchip export price	AUD165/BDMT
Moisture content	48%
Harvest schedule	July 2014 to December 2015
Harvest costs	AUD79.39/GMT (indexed for inflation)
Lease and management fee charged	2A - \$125 pa (non indexed) 2B - \$296.63 (indexed for inflation)
Years of lease and management fees to pay until harvest	2 years
Projected return per woodlot (before L&M fees)	\$232.33
Projected return per grower (after taking into account L&M fees to be paid)	2A – (\$17.67) 2B – (\$344.22)

This Project is more difficult to ascertain the ongoing viability given the different lease and management fee structure of the two parts of the Project. For those growers in Part A there is a projected return of minus \$17.67 per woodlot after taking into consideration lease and management fees to the end of the Project, however, for those growers in Part B, the projected return per woodlot would be insufficient to cover the lease and management fees to be paid until harvest, resulting in a cost to growers of approximately \$344.22 per woodlot.

It should be noted that the calculated returns for Parts A and B assume that each Project is operating. It could not be recommended that Part A continue without Part B, as the cost structure in only operating part of the entire Project, would change the Project economics significantly, resulting in one of either parts of the Project being hugely unviable.

Given this outcome we consider that both parts of this Project to be unviable.

## 6.4 Project 3

Project 3 comprises two different parts: 2000-300 and 2001-300. Each part pays a slightly different lease and management fee, however, the harvest proceeds are pooled together and divided amongst the total growers for the Project. The Project can be summarised as follows:

Location of plantation/s	126 ha at Bremer Bay, 108 ha at Kangaroo Island
Total number of woodlots	234 – 2000-300 comprising 54 woodlots, 2001-300 comprising 180 woodlots
Total projected volume of timber	8,559 GMT at Bremer Bay
Woodchip export price	AUD165/BDMT
Moisture content	48%
Harvest schedule	August 2015 to September 2015
Harvest costs	AUD80.63/GMT (indexed for inflation)
Lease and management fee charged	2000-300 - \$296.63 (indexed for inflation) 2001-300 - \$279.84 (indexed for inflation)
Years of lease and management fees to pay until harvest	3 years
Projected return per woodlot (before L&M fees)	\$95.01
Projected return per grower (after taking into account L&M fees to be paid)	2000-300 – (\$769.81) 2001-300 – (\$720.85)

The projected return is negative for growers in both the 2000-300 Project and the 2001-300 Project, meaning that the projected income is insufficient to cover the lease and management fees to be charged until the finalisation of harvest. Given this outcome, we consider the Project to be unviable.

## 6.5 Project 4a

Project 4a comprises a majority of woodlots at Bremer Bay (188) and a small amount on Kangaroo Island (27). As growers in the Project do not pay lease and management fees, there is no ongoing financial commitment from growers. The Project can be summarised as follows:

Location of plantation/s	188 ha at Bremer Bay, 35 ha at Kangaroo Island
Total number of woodlots	223
Total projected volume of timber	14,206 GMT at Bremer Bay
Woodchip export price	AUD165/BDMT
Moisture content	48%
Harvest schedule	October 2015 to December 2015
Harvest costs	AUD80.63/GMT (Indexed for inflation)
Lease and management fee charged	There are no ongoing lease and management fees
Projected return per woodlot	(\$217.13)

This Project is considered to be unviable.

## 6.6 Project 5a

Project 5a comprises a majority of woodlots at Bremer Bay (188) and a small amount on Kangaroo Island (27). As growers in the Project do not pay lease and management fees, there is no ongoing financial commitment from growers. The Project can be summarised as follows:

Location of plantation/s	95 ha at Bremer Bay, 191 ha at Kangaroo Island
Total number of woodlots	286
Total projected volume of timber	7,942 GMT at Bremer Bay
Woodchip export price	AUD170/BDMT
Moisture content	48%
Harvest schedule	January 2016 to March 2016
Harvest costs	AUD83.05/GMT (Indexed for inflation)
Lease and management fee charged	There are no ongoing lease and management fees
Projected return per woodlot	(\$96.84)

This Project is considered to be unviable.

## 6.7 Projects 4b, 4c, 5b and 5c

These Projects comprise either *E.nitens* or *P.radiata* and are longer-term projects all located on Kangaroo Island. Given our assessment of the uncertain long term future of timber on Kangaroo Island we believe that is highly unlikely that there will be a financial return to growers in these projects and therefore they should be deemed unviable and the Projects ended.

## 6.8 Project recommendation

The following table summaries our review of the viability of the Projects:

Project 1	Unviable
Project 2	Unviable Project 2a – Unviable Project 2b – Unviable
Project 3	Unviable
Project 4a	Unviable
Project 5a	Unviable

Given the above, we would recommend that the Responsible Entity commence procedures for the winding up of the Projects.

## 7 RuralAus' position

RuralAus considers that the market conditions have deteriorated significantly since the update to growers in May 2012 and this Report best represents the current position of the Projects.

In May 2012, Elders Limited decided to exit the industry, which has created further uncertainty and volatility. This has been exacerbated by the demise of Gunns Limited in late September 2012. We believe that further volatility and financial distress is likely to occur over the next 12 to 36 months.

As previously mentioned, the relatively small volumes of timber that RuralAus would be able to export for growers has meant that RuralAus is a "price taker" in the market and the best price that has been offered to RuralAus as at the date of this Report is AUD145/BDMT based on spot shipments into China.

The potential winding up of the Projects has a significant financial impact on RuralAus. In addition to the \$2.7m that RuralAus has invested in the re-establishment and continued ongoing management and maintenance of the various Projects, RuralAus has an outstanding loan receivable from growers in Project 1 totalling \$4.2m. With the potential winding up of that Project, RuralAus will not receive any funds from borrowers and therefore this amount will be written off as uncollectable.

Part of the reason for recommending that we wind up these Projects is because RuralAus believes that growers should not pay ongoing lease and management fees when faced with little or no definitive return. No firm decision has been made by RuralAus on whether it will continue to manage and maintain the plantations at Bremer Bay. There is considerable risk and cost to RuralAus if it continues to pay lease fees as there is clearly no guarantee of the woodchip market improving in the foreseeable future. It is highly likely that RuralAus will not continue to lease the properties at Bremer Bay associated with Projects 2, 3, 4 and 5.

RuralAus will reimburse growers on a pro rata basis the 2012/13 lease and management fees in lieu of the Projects being wound up prior to the expiry of the annual lease and management fee payment period.

2 November 2012

Mr Rob Garton Smith  
Primary Securities Limited  
13 Nairn Street  
FREMANTLE WA

Dear Rob

**Financial Impact on RuralAus Investments Limited ("RuralAus") on Termination of Projects**

I refer to our recent telephone discussions, emails and to the Project Viability Report prepared by RuralAus that recommends the termination of all Projects and take this opportunity to advise of the financial impact termination of the Projects will have on RuralAus.

As you are aware, RuralAus offered non-recourse loans to growers in Project 1. The total principal outstanding in relation to those loans is \$4.2m. Due to the fall in the FOB woodchip price, RuralAus has raised provisions regarding the non-recoverability of these loans totalling \$4m. This resulted in a substantial loss recorded in RuralAus' 2012 Annual report, such that RuralAus' auditors, Ernst & Young, questioned the ongoing viability of the RuralAus Group.

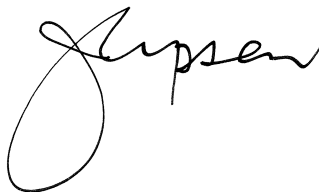
On termination of Project 1, RuralAus will not recover the loans in the Project and therefore will lose \$4.2m.

In addition, in 2005 RuralAus raised \$2.0 in capital from its shareholder base that was applied to the plantations to bring them up to an acceptable standard, following two years of voluntary administration of the Group. An additional \$700,000 of RuralAus shareholder funds have been spent over the past seven years on the ongoing maintenance of the plantations. On termination of the Projects, RuralAus will not be able to recover this \$2.7m.

In summary, RuralAus will lose \$6.9m on the termination of the Projects and therefore I wish to advise from RuralAus' point of view, the decision to recommend the termination of the Projects was not taken lightly, as it will clearly have significant ramifications on our own ongoing viability.

Should you wish to discuss any of the above, please do not hesitate to contact either Scott Wallace or myself.

Yours sincerely



John Ipsen  
Chief Executive Officer  
RuralAus Investments Limited

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