

3.7 Wood Cluster/ Centre of Excellence

| PGF Application | | For: Approval (in principle) | |
|---------------------|--|------------------------------|--|
| Applicant: | Eastland Community Trust (ECT) | Pipedrive ID # | MBIE <small>Commercial</small> |
| Entity Type: | Trust (please provide your Trust Deed) | PGF Funding Sought: | \$19,500,000 |
| Region | Tairāwhiti | Total Project Value: | \$ <small>Commercial Information</small> |
| Tier: | 2 - Sectors | Co-contribution rate: | <small>Comm</small> % |
| Sector: | Wood Processing | Funding Structure: | Grant / Loan |

We recommend that the IAP:

- a) Support** \$19,500,000 from the PGF fund, as an approval in principle, towards Wood Cluster/ Centre of Excellence (WCCE) subject to:
- each tranche of funding sought for individual investment components of the WCCE, be conditional on match funding from the applicant; and
 - draw down on submission of a business case that has been assessed by the PDU.
- b) Note** The 'in principle' decision will allow ECT to accelerate the WCCE, and begin to plan the roll out of the various components, with confidence they have a funding partner.
- c) Note** The PDU acknowledges it does not have the level of detail required to make individual component investment decisions as yet. This will be developed and provided as each component requests a funding tranche. However, the PDU has confidence in the concept following consultation with MPI and the commissioning of consultants Forest Economic Advisors (FEA) to undertake a 'Spotlight Paper' (more fully described below).
- d) Note** The level of funding recommended matches that requested by the applicant.
- e) Note** Funding should be granted on an equal basis (T&Cs) to that provided by ECT. The IAP should note co-funding will be a mix of new capital from ECT, an acknowledgment by the PDU that ECT has provided \$ Commercial to Far East Saw Mill (FESM) over the last six months to ensure operating expenses were covered (accepted by the PDU as part of ECT's co-funding), and possible investor capital as project components are developed in the future.
- f) Note** The applicant has proposed a ten year facility with an annual renewal until fully drawn down.
- g) Discuss** The WCCE. This project is an election manifesto promise made by Labour pre the 2017 election. \$ Commercial dollars was promised to Tairāwhiti for wood processing. The original concept was for prefabricated homes to be built. Following more detailed analysis by the region, processing logs and manufacturing components for the building industry were identified as options that would generate stronger productivity outcomes. The funding was to be released on the basis of:
- I. Match funding by the applicant
 - II. The provision of a business case

Proposal:

- Consider the following:
 - The PDU has worked with the applicant over the past year on this project. This funding is for shovel ready projects associated with the development of the WCCE.
 - Certain components of the wider programme, while being shovel ready, are pre-commercial, making access to commercial funding difficult.
 - The funding is divided into tranches associated with various components of the programme. These include:
 - Wet Plant 1 Completion. Total cost estimate: \$ [redacted]
 - Sawmill Enhancements. Total cost estimate: \$ [redacted]
 - New Drystore with Floor Space for Thermal Modification. Total cost estimate: \$ [redacted]
 - Thermal Modification Plant. Total cost estimate: \$ [redacted]
 - Woodwaste Processing. Total cost estimate: \$ [redacted]
 - Container Shipping. Total cost estimate: \$ [redacted]
 - WET Plant 2 Building. Total cost estimate: \$ [redacted]
 - Combined Heat and Power Plant Total cost estimate: \$ [redacted]
 - The WCCE is being developed to increase the value add proposition to the region via increased processing of logs from current levels of [redacted]%, thus generating more economic benefits to the region.
 - Public benefit of this programme comes in a variety of forms including increased jobs, training, and value chain development not currently realised.
- The first two projects to be undertaken via this programme are proposed to be:
 - Wet Plant 1 Completion. Total cost estimate: \$ [redacted]
 - Sawmill Enhancements. Total cost estimate: \$ [redacted]
- To help analyse the opportunities and programme components associated with the WCCE, the PDU has contracted Forest Economic Advisors (FEA). They have been conducting and producing studies and papers (Spotlight Papers) for the PDU to help inform decisions relating to forestry and wood processing. FEA has met with Eastland Community Trust, Far East Saw Mill and Wood Engineering Technology (WET) (key partners in this application). FEA has produced a 'Spotlight Paper' that provides positive analysis of the opportunities associated with developing the Wood Cluster/ Centre of Excellence. Please find this paper as Annex 2.

Assessment against the PGF criteria:**Eligibility Criteria**

- This application is eligible for PGF funding. That said, it must be noted that individual tranches of funding must be approved with, match funding from ECT or private investment, and on provision of a business case and assessment of that business case by the PDU. Programme components that are established to undertake commercial activity, generating revenue, are expected to attract funding via the development of a loan.

Productivity Potential

- The components associated with the WCCE are designed to **lift productivity** in the region by significantly increasing the regional processing of logs felled in Tairāwhiti. The region has a well-established supply of raw material that has a well understood harvest profile, verified by Ministry for Primary Industries (MPI) and FEA.
- The programme will generate direct FTEs with various components requiring staffing levels to construct, operate, maintain and manage assets. Exact figures will be developed with each programme component and be part of the business cases.

| Policy objectives and regional priorities | | |
|---|---|-------------------|
| <ul style="list-style-type: none"> The project has strong regional support evidenced by Eastland Community Trust being the co-funder of the programme. The industry is a key economic driver in the region, as outlined in the Tairawhiti Economic Action Plan (TAEP). | | |
| PGF Criteria | Assessment Commentary | Rating (0✓ to 5✓) |
| Link with fund and government outcomes | | |
| Creates permanent jobs | <ul style="list-style-type: none"> Each individual component will seek to generate jobs either directly or indirectly. Examples of each are: Direct increase in jobs through Saw Mill Enhancements, designed to take Far East Saw Mill from a single shift model (current status <small>1000</small> FTEs) to double shifts, with an addition of <small>1000</small> new FTEs. The establishment of the New Drystore with Floor Space for Thermal Modification will be an enabler via the creation of a facility that will in part, house the upgraded Thermal Modification which will require new FTEs to operate | ✓✓✓✓ |
| Delivers benefit to the community | <ul style="list-style-type: none"> The wider industry is a significant driver of economic activity in the region. At present, only <small>1000</small>% of logs are processed in Tairawhiti. The loss of economic activity/ opportunity is reducing the potential benefits to the community that would accrue as additional opportunities to create value add were realised | ✓✓✓ |
| Increased utilisation and returns of Maori asset base | <ul style="list-style-type: none"> Maori are significant owners of forestry in Tairawhiti. However, increased returns are not guaranteed as feedstock prices are likely to be controlled by market forces | ✓ |
| Enhanced sustainability of natural assets | <ul style="list-style-type: none"> An argument can be made that sustainable felling and planting of forestry blocks addresses this criteria but the WCCE is only one aspect of this wider model | ✓✓ |
| Mitigation of climate change effects | N/A | |
| Additionality | | |
| Adding value by building on what is already there | <ul style="list-style-type: none"> The WCCE is being established on a hub and spoke model with FESM and WET at the Hub. Both these operations are currently in place. Their scale up and enhancement will build on existing assets | ✓✓✓ |
| Acts as a catalyst for productivity | <ul style="list-style-type: none"> The goal of increasing the processing percentage of | ✓✓✓✓ |

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| potential in the region | logs felled in Tairāwhiti and as a result climbing the value chain, will act as a catalyst by increasing economic activity. The establishment of new processing components at the WCCE site will further act as a catalyst and help in the development of an integrated end to end process, all of which will help to increase the productivity potential of the WCCE | |
| Connected to regional stakeholders and frameworks | | |
| Alignment with regional priorities | <ul style="list-style-type: none"> Forestry and related services is a well-established regional industry and has been identified in the Tairāwhiti Economic Action Plan as a priority. The fact that the project partner and co-funder for this programme is ECT provides additional evidence of regional support | ✓✓✓✓ |
| Support from local governance groups (inc. Councils, Iwi/Hapu) | <ul style="list-style-type: none"> As above | ✓✓✓ |
| Governance, risk management and project execution | | |
| Robust project management and governance systems | <ul style="list-style-type: none"> ECT has noted it will be heavily involved in the Management and Governance (M&G) of this programme. They own the land on which FESM and WET are situated. They will be match funding the PGF and so have considerable interest in ensuring the programme meets goals, deliverables and milestones. FESM has management in place and have overseen the recommissioning, training and upgrading to date. WET ownership and management also has strong industry experience | ✓✓✓✓ |
| Risk management approach | <ul style="list-style-type: none"> The programme will be overseen by ECT and the PDU. On the ground MPI will undertake periodic site visits to monitor component progress. This has begun with the PGF funding \$500k to FESM through a separate application. MPI has conducted site visits to ensure deliverables have been met and has provided positive reports on the works to date. Each new component seeking a funding tranche will be subject to a business case. Additionally, the PDU has contracted Forest Economic Advisors (FEA) to conduct a 'Spotlight Paper' on the WCCE. The report confirmed opportunities existed to increase processing in the region that would be enabled by the components being proposed in this application | ✓✓✓ |
| Future ownership / operational management | <ul style="list-style-type: none"> Individual programme components will likely have different ownership models. ECT owns the land the WCCE sits on. Discussions have been had with ECT | ✓✓ |

about possible investor interest in building infrastructure on site. Equally, Eastland Group, ECT's commercial arm might have an interest in the containerisation component as they own and run Gisborne Port. Options will be more fully analysed as each component is developed

Analysis of the benefits and costs

A summary of benefit analysis conducted:

- Tairawhiti has an acknowledged 'Wall of Wood' requiring felling and processing across the next five to ten years (see Annex 1 ECT Letter). This will be followed by continued annual forestry activity going forward. As such, an opportunity exists to increase the processing value of that windfall. To take advantage of this opportunity investment is required that is in excess of that available in the region. Investment has been secured with the recommissioning of FESM by its parent company Spectrum, and by ECT and WET's investors.
- The direct benefits of the continued establishment and growth of the WCCE will be two fold. First, jobs. New FTEs will be created through several of the programme components of the WCCE. Second, an increase in the economic benefit of the industry to the region by processing more of the logs felled in Tairawhiti.
- If the life of the assets is used as a metric, the level of funding against the jobs created and economic activity undertaken is strongly favourable with a number of assets having a ten, twenty or thirty year lifecycle.

Financial Analysis

The PDU has commissioned a Spotlight Paper. This is part of a contract undertaken by the PDU to analyse aspects of wood processing and forestry in New Zealand. The work has been undertaken by Forest Economic Advisors (FEA). Their report on the WCCE is attached as Annex 2. It should be noted that while the package of funding is \$19.5m, each component of the funding will not exceed \$^{Commercial} [REDACTED], and will require a business case for each tranche.

Funding Arrangements

The complete funding package is not known at this stage as each component of the programme will be dependent on the submission of a business case. The PDU has discussed possible funding models with ECT and has agreed that funding will be provided on the same terms as the co-funder (ECT). It is envisaged that programme components will usually attract a loan, unless specifically not revenue generating.

This Cover Sheet is seeking an 'in principle' recommendation to approve that will be followed by Cover Sheet development for the IAP of each programme component as business cases are submitted to the PDU.

Due Diligence and Ownership

ECT is an independent Trust established by Gisborne District Council (GDC). GDC appoints all Trustees to ECT. GDC is the sole capital beneficiary of the Trust. GDC is not the income beneficiary. The Trust has an eighty year Trust Deed. Following the 80 year period, all Trust assets will revert back to GDC.

Far East Saw Mill has had Due Diligence completed through its earlier application for \$^{Commercial} [REDACTED].

Wood Engineering Technology has had Due Diligence completed. It is noted that IAP member John Rae is a

Director of WET.

As this application is to approve in principle funding to be placed alongside ECT, DD is focused on ECT. This is being completed at present.

Trustees ECT:

- Michael Muir
- Meng Foon
- Te Rau Kupenga
- Dr Paul Reynolds
- John Clarke
- Dr Jillian Chrisp
- Ailsa Cuthbert

Key Management Personnel:

- Gavin Murphy (CEO)

Risk Assessment

The key risks to the PDU and proposed mitigations of this investment are as follows:

| Type of risk | Risk description | Mitigations | Risk Rating L/M/H |
|--------------|------------------------|--|-------------------|
| Slippage | Commercial Information | <ul style="list-style-type: none"> • Commercial Information | Med |
| Market | Commercial Information | <ul style="list-style-type: none"> • Commercial Information | Med |

| | | Commercial Information | |
|------------------|--|--|--------------------|
| Expansion | FESM. Plant upgrades are required to extend the operation and undertake double shifts. Operational expansion always carries risk. Commissioning a scale up will come with a loss of productivity, as will training of new staff. | <ul style="list-style-type: none"> Pricing for components is well understood and demand for the service is well established. Management has trained staff in the last 12 months and has experience in running the facility. | Med |
| Programme | Additional risk is acknowledged in relation to the various programme components. The type of risk and level will be better understood as the business cases are developed. | <ul style="list-style-type: none"> Mitigation of the risks associated with programme components will be addressed in the development of the business cases. | Unknown at present |

Consultation undertaken or implications:

FEA has been consulted and contracted. Their report has been submitted to the PDU (Annex 2).

MPI's Tairawhiti team have been involved in this application and have considerable knowledge of programme components including Far East Saw Mill and Wood Engineering Technology. They will continue to be strong programme assessment team members. MPI have concerns in relation to the industry, noting the volatile nature of it. In relation to the material provided to date they note a lack of evidence of the market, providing concerns the programme is not addressing market pull, instead focussing on supply. The PDU believes this is valid. The PDU has spoken to MPI and has outlined that no programme component will be agreed to without a business case. MPI has agreed with this approach.

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| Supporting proposal: | Yes |
| Appendices: | Yes. Annex one: ECT letter. Annex two: Spotlight Paper |
| Author of paper: | ELH |