Response to:

Proposed Taxation Arrangements for Plantation Forestry

To:

Review of the Taxation of Plantation Forestry
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From:

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1 Introduction

Managed Investments Schemes (MIS) are the single biggest capital raising exercise for Australian Agribusiness annually. Within the MIS sector, the largest pool of capital is raised by the Timber Sector. Over the last 10 years, in excess of 800,000 hectares of new plantations have been established in Australia, which at harvest will provide a substantial and ongoing resource meeting the Government’s 20/20 plantation vision and providing for billions of dollars of export income.

Quite apart from the direct employment created by full time and contractor employees in the forestry sector, the reach of MIS into the shareholders of the listed players in the Timber MIS area is substantial. The listed players in the Timber Sector have over 75,000 shareholders and over 43,000 direct investors. Overwhelmingly these investors are city based people who are committing their capital to forestry projects.

Australian Agribusiness Group (AAG) provides research services and rates investment products. AAG is the market leader in the field of providing research in to the Agri MIS Sector and undertakes a comprehensive level of research into the products which it rates. This includes a Corporate Governance Review (undertaken in an alliance with Ernst & Young), a review of track record and a review of the current offering. Each of these sub sections are separately rated and then with a risk return overlay an overall rating is provided to these projects. The ratings substantially affects the performance in the market of the entity seeking to raise funds for the forestry project.

The Australian Agribusiness Group has also lead the market in every significant innovation in research and rating of Timber and other Agri MIS products over the last six and a half years. This includes dynamic release of research, the provision of detailed market overviews for all of the major MIS Investment areas, a comprehensive web page which includes fundamental research on every MIS product and detailed research on those products which we have researched, sortable tables to assist financial planners to make reasoned and sound decisions on behalf of their investors, the only authoritative survey of capital raised in the sector (attached to this report) and substantial supporting research around the performance of the Agri and/or MIS Sector and other sectors of the economy. AAG also compiles and distributes the AAG Agri Index which is a measure of the performance of listed Agri Businesses against the All Ordinaries Index in Australia.

AAG’s Agri MIS Research and Ratings are distributed by Standard & Poor’s. AAG’s own distribution extends to over 10,000 industry professionals, media and the public.

2 Background to MIS

AAG is supportive of the MIS Sector in that it has provided impetus for the re-awakening of agriculture in Australia as an investment option. Australia lags behind the US, the EU and the UK in its recognition of the Agri Sector as a place for investment. The result is that Superannuation Funds, individual Investors and the wider investment community have, for the most part, little exposure to the Agri Sector, a part of Australia’s economy in which there is a comparative, competitive and sustainable world advantage.

This sector lacks capital in order to achieve scale which then allows it to become internationally market relevant. Over the last 20 years investment in large scale Agriculture has been piecemeal, disorganised, focused on large scale corporate investment and not available in effective parcels to the average investor.
The MIS Sector has provided access to individuals into Agricultural and Forestry Investments in Australia.

The maturity of the MIS Sector has advanced substantially over the last 6 years and the quality of offerings has significantly improved. In general terms, the entities which are making the offerings, particularly in the Timber industry, are more professional, better organised, more environmentally conscious and more likely to produce a sound return for investors today than they have been at any time in the past.

To date, although heavily regulated and scrutinised, the MIS industry has had a relatively stable period of Government intervention. On the back of this stability, the sector has improved its performance and grown the amount of capital it has attracted. AAG believes that to increase the level of complexity, bureaucracy, compliance or to add additional layers of external scrutiny would be counter-productive, not just for investors (who would ultimately wear the increased costs) but particularly for the Federal Government where ultimately, harvests proceeds and the Government's potential tax take will also be reduced.

We’re confident that the Federal Government’s aim in this review of MIS Forestry projects is to produce a system which is better than currently exists, rather than a system which is more complex, less workable, less efficient and less friendly to investors, the Government’s revenue targets, the environment and other policy objectives such as the Plantations 20/20 Vision.

3 Addressing the Proposed Changes to Forestry Taxation Arrangements

3.1 New income tax law governing the deductibility of investments in MIS

AAG sees no reason to change the existing taxation structures for Forestry MIS projects.

Our reasons may be summarised as follows:

- Investors in these projects are clearly and fundamentally in the business of growing trees.

- Investors in these projects are clearly exposed to the risk of growing these trees both from the rate of growth, their exposure to climatic factors, their exposure to management skill and attention, their exposure to location, and their exposure to market prices.

- The combination of these investor exposures amounts to risk. The acceptance of this risk by investors clearly demonstrates that they are in the business of Forestry.

- There is no detailed proposal on the table from the Government in terms of the variation to what currently exists. The lack of a proposal creates substantial uncertainty and has the potential to affect long term market relationships with the trading partners involved in the acquisition of the outputs of Forestry. These trading partners seek consistent, long term supplies of product. Uncertainty will reduce future plantings and create future breaks in supply. These breaks in supply provide opportunities for Australia’s international competitors to acquire market share which is difficult to regain. Further, it swings price negotiation advantages to the buyer, putting at risk future investors. Uncertainty in the industry will also be characterised by an inability to access appropriate management, a lack of willingness to invest in infrastructure and facilities, a corresponding flow-on affect through contractors and related parties to the Forestry Sector will be reluctant to invest in the future where the future is uncertain.
• The existing system works well, is proven to work well, has a track record of performance and we see no reason to change something which is performing to these characteristics.

• The system as it currently stands provides for clarity, certainty and the ability to plan and invest with confidence. Any action which is counter to this would be to fly in the face of sensible investment as it is applied to most other sectors of the economy.

3.2 Deduction cap of $6,500 per hectare

The concept of placing a cap on the deductibility of investment projects is strongly opposed by AAG. And our reasons may be summarised as follows:

• The Cap shows a fundamental lack of understanding of investor needs. It seeks to apply a “one size fits all” outcome for investors. Investors are not “one size” and the proposal will not “fit all”. In fact the proposal is likely to harm many investors, if not all investors, and create precisely the opposite effect of what may be intentioned.

• Risk vs Return is a key determinant of why investment is made. Applying the Cap assumes that all risk and all return is assumed to be equal. This is absolutely not the case. Some Investors seek reduced risk and are prepared to pay an additional cost in order to achieve the reduced risk. Other Investors have a different view. Some Investors take the view that long term outcomes are acceptable in their investing time frames. Others do not. The structure of various investments as they are offered matches with the personal requirements of Investors’ needs as determined by Financial Planners or Advisors. Applying a Cap will tend to remove the capacity to tailor solutions to meet individual investors needs.

• In any decision to apply a Cap in the first year it is likely that any additional costs will be charged to the Investor in the second year. In reality the cap will produce a one off impact but no long term impact for repeat investors. It is likely that promoters will charge ongoing fees and/or restructure their projects in such a way as to ameliorate the impact of the Cap. The result may be that the impact of the Cap will be counter-intuitive to the rationale behind the cap. That is, Investors will end up paying more per hectare of Forestry planted.

• The cap runs contrary to the Government’s 20/20 Vision for Plantation Forestry. It flies in the face of regional forestry agreements which are seeking to lock up additional areas of native forest and place increased pressure upon plantation forestry resources. The Cap is hence likely to be anti the Government’s longer term environmental goals which seek to place less reliance on native forests and more reliance on plantation. Placing a Cap will likely reduce the attractiveness for the production of investment products and hence reduce the amount of plantation forestry which is established.

• A Cap is fundamentally anti – free market. There is no way of getting around this concept. What the Government is saying is that it has the right to determine the cost, the structure and the profit which is available to promoters of Timber MIS products. This level of intervention of private enterprise is surprising as a potential policy of this Government.
There are a large number of Timber species which are grown under the MIS banner. These include both long and short rotations of a number of varieties of Eucalyptus, Sandalwood, Teak, Mahogany, Paulownia and Pine. Each of these species have different costs structures both in terms of establishment, ongoing maintenance and harvest times and costs. It is fundamental that an MIS promoter needs to have flexibility in pricing these products. Applying a Cap will be to destroy the flexibility and more importantly to destroy the higher value timber species which for the most part will be directed into higher value, higher employment end users.

The impact of the Cap will likely lead to promoters seeking to reduce their spending in order to maintain their profit margins. Reduction of costs will ultimately be felt in the plantation forests which are established. In turn, this will have the impact of reducing the performance of those forests, increasing the risks to investors, decreasing the likely harvest returns and decreasing the potential future taxable income of investors. The Cap is therefore counter-intuitive to the goals of the Federal Government.

3.3 Extension of planting period from 12 to 18 months
The Australian Agribusiness Group is supportive of the concept of extending the planting period from 12 -18 months. We are supportive because this extension takes into account seasonal variations and is reflective of good silver cultural practice.

AAG is supportive of the variations to programs which create a improvement in the existing situation and provide for improved certainty, decreased risk and better Agricultural outcomes.

3.4 Trading in forestry MIS investments
AAG is strongly supportive of the need to provide a secondary market in Timber Investments in Australia. However we have some variations and comments to the proposal as it is presented. These are set out below:

- AAG believes that the initial holding period by Investors should be extended to 8 years (not 4 years) to encourage investment for the right reasons.

- Further we believe that an 8 year period will provide a more sensible secondary market for these investments because:
  - At 8 years it is possible to make a sensible assessment of current and future yield and therefore future value which then provides for a sensible basis for assessing the value of the transaction. The value of the transaction is likely to be more in the investors favour than at 4 years where such an assessment is not possible.
  - At 8 years, because the shorter rotation plantations are 2-3 years away from being harvested, investors will have more reason to hold on rather sell and therefore the transaction on price will be more balanced on one made at year 4.

- We see that the secondary market should be applied from today, inclusive of those plantations which are already 8 years of age rather than moving forward from this point in time and the beginning when this years plantings become 8 years old.
• We see that there needs to be a clear process established which is verifiable and transparent for the evaluation of plantations in order to protect investors and to ensure future tax revenues for the Federal Government are preserved.

• We believe that a secondary market on this basis (8 years minimum holding period) would encourage longer rotation plantation forestry which aligns more appropriately with the Government’s 20/20 Vision for Plantation Forestry. Investors will know they have an option after 8 years to sell or to continue to hold with regular reviews of their holding position.

• Longer rotation forestry will further ease pressure off native forests have a positive environmental impact and support the Government’s policies in these areas.

• Longer rotation forestry, in balance with shorter rotation woodchip forestry, will provide for a sustainable industry and will both reduce Australia’s current trade deficit for imported structural timber and build our market dominance in both long rotation and short rotation export timbers.

3.5 Certification of MIS companies
The Australian Agribusiness Group is fundamentally opposed to additional certification of MIS Forestry Companies. Our view is that the levels of certification which currently exist are ample and an additional level of certification will add a level of cost which is anti investor, anti future revenues and anti good Forestry.

The industry already has significant levels of certification through State based Codes of Practice, the FSC/AFS systems, the ASIC, the ATO and through at least 3 research companies (including AAG). In addition to this level of scrutiny are the Compliance Committees required under the Managed Investments Act, the use of independent Foresters, the extensive use by MIS companies of web pages and newsletters to their investors communicating the outcomes of independent Foresters and other reviews and the public disclosure of historical performance of investments (for example through AAG’s track record review).

Increased compliance will create increased costs and this in turn will decrease Australia’s competitive position in relation to export of forest products. Increased compliance will also decrease returns to investors and future tax revenues for the Government which appears to be counter-intuitive to the purposes of this review.

3.6 Administration of the goods and services tax (GST) for MIS
The Australian Agribusiness Group is supportive of an improvement in the simplicity of the administration and application of GST to Investors in Forestry MIS Projects.

3.7 Review of arrangements in 2011
The Australian Agribusiness Group is supportive of a review of arrangements in 2011, where the secondary market may be established on the basis that we have set out above. That is, with a minimum holding period of 8 years AND where the secondary market includes those trees which are already 8 years old rather than starting from today. In the event that a secondary market is forward looking rather than accepting the current situation, we see that a review would be more appropriate further out rather than in 2011.
4 Summary

AAG believes that consistent policy, certainty of outcomes for the industry and for Investors and policies which are supportive of good silvicultural practice are all essential to the industry. We believe that the Government's view will be to reinforce a process which encourages sensible investment, protect the interests of individual investors whilst allowing them choice and management of their risk return paradigms, and preserves future taxation revenues for Treasury.

We look forward to clarifying and expanding on any area above.

5 The Author – Australian Agribusiness Group

Australian Agribusiness Group (AAG) was formed in 1997. It provides agribusiness, research, investment and management skills to smart agribusinesses.

AAG is the market leader in research into the agri MIS sector. In alliance with Ernst & Young, it provides detailed research and rates product offerings and supports the sector with a range of decision making tools. Its research reaches over 140 financial planning groups, covering some 9,000 financial planners. AAG’s ratings are also distributed by Standard & Poor’s.

AAG provides research to other high growth agribusinesses, manages Stocklease Pty Ltd, provides investment and management services and operates a national consulting practice.

AAG also produces the Agri Index, a measure of the relative performance of ASX to listed agribusiness.

For more information about the AAG please visit www.ausagrigroup.com.au.

6 Appendix 1 – AAG’s End of Year Round Up Report

See following pages.
Introduction and Methodology

- Agribusiness is a massive contributor to GDP. The farm dependent economy was 12.1% of GDP in 2003/04.
- AAG identified all project managers that raised capital in 2005/06 and sent each a written survey.
- Survey responses were collected on the basis that information was confidential if requested and that no one project in particular could be identified from this report.
- AAG received a response from 100% of projects and companies.
- This is the only accurate, precise and comprehensive survey of the capital raising performance of the agribusiness MIS industry undertaken for the 2005/06 financial year and extends on similar reports undertaken by AAG over the previous 4 years.

Number and Type of Projects

- AAG identified 68 agribusiness investment offerings available in 2005/06 compared to 65 in 2004/05.
- Of the 68 investments in 2005/06, 56 were released in that year with the balance continued on from 2004/05. The number of new projects was up 19% from the previous year.
- Timber products represented 32% of products on offer, which was a decrease from the previous year.
- The number of horticultural products available in 2005/06 doubled from the 2004/05 levels.
- AAG identified 27 agri-sectors available for investment with many new horticultural crops now available.

Capital Raising

- The agribusiness investment industry raised $1,141 million in 2005/06, an increase of just 11% on the $1,024 million raised in 2004/05.
- Timber investments received 61% of the investment dollars. This was a decrease in both the capital raised for Timber and the proportion Timber represented of the total capital raised.
- There were large increases in capital directed towards horticultural investments.
- The average investment was $44,000 per investor, down from the previous year. More people invested in the sector with 32,000 investments in 2005/06 compared to 27,000 in the previous year.

Companies

- AAG identified 39 product managers offering investments in 2005/06, with 32 of these continuing on from the previous year. Of these, 60% raised more in 2005/06 than they did in 2004/05.
- Product managers that are part of ASX listed groups represented 23% of the companies and raised about 80% of the capital from 35% of the projects.

MIS and the Economy

- MIS sales follow the cycles of ASX listed equities – there is a 90% correlation with the returns from the All Ordinaries Accumulation Index.

Revenue, Tax and Finance

- An estimated $510 million will be received by investors as tax refunds but we estimate that these refunds will be far outweighed by the tax that is generated from the activity of these projects and the tax paid on future income generated by at least 3 times.
- Future gross income from the projects established for the five years from 2001/02 to 2005/06 is estimated to be $16.4 billion at the farm-gate. The 2005/06 projects will contribute $5.5 billion.
- Approximately 69% of investors geared their investment.

Flow-on Effects

- Western Australia will receive the largest proportion of the new project development by area and Victoria by capital raised (based on area to be developed).
- Around 84,300 ha of timber plantations will be established as a result of the capital invested along with 5,400 ha of horticulture, 1,500 ha of olives and 600 ha of viticulture.
- 69,000 ha of the timber plantations will be hardwood woodchip (e.g. blue gum, acacia) which is a decline of 24% on the previous year.
- Approximately 1,700 people are employed directly by the operators of the 2005/06 projects and 7,000 on a contract basis with more than 400 new jobs being created as a result of this year’s capital raising.
1. Introduction

Agribusiness is a massive part of the Australian economy and contributor to regional growth.

Agribusiness currently accounts for less than 5% of GDP although the real output in agricultural products increased 250% from 1963 to 2003, an average growth of 2.4% p.a. The agri influenced economy contributes $200 billion to Australia’s economy, accounting for 12.1% of GDP (2000/04) 1.

Employment in the Australian agricultural industry has declined with technological advances resulting in fewer people being employed. Currently, 4% of the national workforce is behind the farm gate. Food manufacturing is the second largest manufacturing sector and employer within Australia, employing 20% of the manufacturing workforce 2.

The top 25% of farmers see consolidation as a necessary strategic move to remain viable and competitive in the Australian (and global) agricultural industry. Hence, there is an increasing level of corporatisation in the Australian agricultural industry. This trend has seen a move away from traditional farming, into precision agriculture with today’s farmers using scale and technology to remain at the cutting edge of proven agriculture.

Managed Investment Schemes (MIS) tend to be at this leading edge of technology and are part of the wider industry corporatisation contributing substantial investment, regional growth and significant job opportunities for the rural economy.

AAG has been producing our End of Year Round-up Report on the MIS industry since 2001/02. This current report for the 2005/06 year builds on the previous four years of solid data with another year of detailed information.

2. Methodology

Step 1: AAG produced a list of managers and their projects which were thought to have raised capital in 2005/06. By personal interview, the list was refined to those that released an offer document to market in that year.

Given that not all projects close by 30 June, some of the investments on offer in 2005/06 were investments that were actually released in 2004/05. For these investments we were only interested in the portion of the project’s capital raising that was undertaken in 2005/06. We note however that the majority of products included in this survey were released in 2005/06.

We are interested in both retail and wholesale offerings that offer investments through Product Disclosure Statements (PDS) and Information Memorandum (IM) respectively. Most of the investments in 2005/06 were through the retail form. While many of the wholesale investments are also able to be easily identified and product managers found, others are discreet non-public offerings. AAG was only interested in the wholesale investments that were more public offerings with their IM’s publicly obtainable.

Step 2: Each product manager was sent a survey form and responses were collated and analysed.

AAG is very careful in maintaining confidentiality for those groups that do not want their information to be identified publicly. Amalgamation of data into categories is one of the ways we ensure this.

AAG relied on the honesty of the product managers in completing the survey accurately. Due to the confidentiality of the surveys, the accuracy of information provided is considered to be of a high level.

AAG does not rush to collect the data from product managers which is important in producing a report which is based on information which is collected in a standardised basis. We do not include GST and ongoing management fees.

Step 3: The information is collated into a report for public release.

AAG believes our methodology provides for an accurate analysis of the agribusiness investments industry enabling a very good comparison between years.

3. Responses to this Survey

AAG identified 39 project managers that offered investments in 2005/06.

AAG received responses from 100% of these companies meaning we received information on all of the projects operating in 2005/06.
4. Number and Type of Projects

In the 2005/06 financial year there were 68 projects that raised capital with 12 (17%) of these being projects that continued over from the 2004/05 financial year. The remaining 56 projects were released in 2005/06 (Figure 1) representing an increase of 19% in new projects released year on year.

In the previous year (2004/05) there were 65 projects on offer including 47 projects released in that financial year and 18 projects (27%) continuing on from the previous year.

The success of the 2004/05 year was highlighted by the fact that many projects filled their subscriptions and closed by 30 June 2005. So it is not surprising that given the large amount of capital raised in 2004/05 there were less projects continuing on into the 2005/06 financial year.

Of the 68 projects on offer on 2005/06, 6 of these were wholesale offerings with the balance being through retail PDS.

In addition to the number of projects included in Figure 1, 3 offerings went to market but did not raise any capital during the year. We understand that at least two of these are likely to raise capital post 30 June 2006.

It would be simple to conclude that the growth in the number of projects has come from projects being released by new entrants attracted into the market following the success of previous years. While there were 7 new operators in 2005/06, 4 product managers from 2004/05 did not release a project in 2005/06. Hence, in 2005/06 there were 39 product managers compared to 36 in 2005/06 which we consider to be minimal change. So, as the number of product managers was reasonably stable the growth of projects came from the existing operators releasing more projects each, rather than from more operators in the market.

In 2005/06, the growth in new projects was generated by the horticultural sector where the number of newly released projects more than doubled to become the second largest industry by available investment offerings (Figure 2).

Timber projects again were the largest industry with approximately one third (32%) of the products available (Figure 2).

The Other and Wine/Grape categories had 20% and 18% of the projects that raised capital while the Olives category had 9% of the projects (Figure 2).

The Other category included projects in the following agri-sectors:

- Abalone;
- Cotton;
- Cropping;
- Diversified;
- Infrastructure;
- Livestock (including beef cattle and chickens);
- Pearls; and
- Truffles.

Since AAG started producing this report in 2001/02, there has been a steady increase in the number of projects released (Figure 1) with the 2005/06 year showing a larger increase than in the previous years.

![Figure 1](https://example.com/image1.png)

**Figure 1** Number of newly released agribusiness offerings by year and industry.

![Figure 2](https://example.com/image2.png)

**Figure 2** Proportion of 2005/06 agribusiness offerings that raised capital by industry.
Figure 3 details the very broad range in projects offered in 2005/06. There were 27 agri-sectors recorded by AAG in 2005/06 compared with 24 in 2004/05 (Figure 3). A significant number of sectors had only one project offering investment.

As per last year, woodchip and wine grape projects dominated, but interestingly in 2005/06 wine grape projects overtook woodchip projects with the largest number of offerings. However, as illustrated later in this report (Table 1) wine grape projects contributed just 5% of the capital.

Figure 3 Number of total products on offer in 2005/06 by agri-sector and year of release. (Note: this chart includes the 3 projects that did not raise any capital in 2005/06)

There was an increase in the number of almond projects on offer from 3 projects in 2004/05 to 5 projects in 2005/06. New agri-sectors available for investment in 2005/06 included:

- Apricots;
- Avocados;
- Cherries;
- Macadamias;
- Tomatoes;
- Water; and
- Walnuts.

Interestingly, these are mostly horticultural projects.

5. Capital Raising

In total $1,141 million was raised in 2005/06 for agribusiness MIS (Figure 4). This was an 11% increase on the 2004/05 year, and considering the amount of new projects and the strong performance in the general economy (Figure 10), is a lower result than we would have expected.

Figure 4 Capital raised in the agribusiness investment industry over the past seven years (Note: 1999/00 and 2000/01 figures are estimates only while all other years are determined from AAG’s end of year surveys).

There is certainly a distinction between AAG’s survey results and an estimate produced by another researcher where it is evident that an additional $164 million of future revenues for one particular product manager has been included in the estimate of total capital raised. It was also evident from that data that GST had been included for some companies but not for others. AAG’s methodology provides a more accurate and precise measure with comparisons between years to be more easily undertaken. All data is collected on a standardised basis with GST excluded and only capital actually paid in the year included. The dollar figures of capital raised included in our report are the dollar amounts actually raised in 2005/06. AAG has not included any commitments for future payments as it is too difficult to distinguish between what is development and ongoing management fees.

Table 1 details the breakdown of the capital raised by industry based on 100% of the surveys we sent.

<table>
<thead>
<tr>
<th>Table 1 Capital raised by industry</th>
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<tbody>
<tr>
<td>Horticulture* $181m</td>
</tr>
<tr>
<td>Olives $73m</td>
</tr>
<tr>
<td>Timber $698m</td>
</tr>
<tr>
<td>Wine/Grape $62m</td>
</tr>
<tr>
<td>Other $127m</td>
</tr>
<tr>
<td><strong>TOTAL</strong> $1,141m</td>
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Note: The category Horticulture excludes olives.
Note: Figures have been rounded.
Timber again took the bulk of the capital, but there was a decline of 9% in the amount invested in timber projects (Table 1). The proportion of total capital raised by Timber projects compared to total sales also declined; Timber was 61% of all sales in 2005/06 (Figure 5). As a proportion of total MIS sales, Timber is at the lowest levels for at least the last five years (Figure 5).

It is not surprising that sales in Timber projects declined as a proportion of the total given that the proportion of Timber projects on offer has also declined. In 2005/06 they were 32% of available investments compared to 52% in 2003/04, when Timber sales were at their highest levels of the last five years in terms of proportion of capital raised (Figure 5).

The capital raised for Horticultural and Olive investments increased by 124% and 114% respectively compared to 2004/05 sales and combined increased from 11% of sales in 2004/05 to 22% of sales in 2005/06 (Table 1). These increases have come on the back of 100% and 67% increases in the number of products available in the Horticultural and Olive categories respectively (Figure 1). Horticultural and Olive projects combined represented 30% of the new products released in the year (2005/06) (Figure 2) compared to just 19% last year (2004/05).

There was also a decline in sales for Wine/Grape projects down to just $62 million. Sales in the Other category increased by 105% to $127 million (Table 1).

The major agri sub-sectors saw some varied changes year on year as Figure 6 illustrates.

Of the $698 million sales for Timber investments in 2005/06 woodchip projects received $532 million which was the bulk (47%) of total capital raised but was a 13% decline (Figure 6) on the previous year.

Pine/eucalypt sawlog projects and other specialist/high value timber projects (e.g. teak, mahogany etc.) saw an increase of 12% and 8% respectively (Figure 6).

Livestock projects such as beef and chickens had a massive increase in capital raised by 836% from a relatively low base, while almonds increased by 183% to $120m (Figure 6).

Figure 7 outlines the average of the average project investment by industry. Across all projects, the average project investment was $44,000 per investor with the median being $36,000.

The fact that the average is greater than the median indicates that a couple of products with large average investments brought the average up.
While the total amount of capital raised increased in 2005/06, both the mean and median decreased meaning that more investors invested in agribusiness MIS offerings in 2005/06 than in 2004/05. The total number of investors was close to 32,000, representing an increase of 19% on the 2004/05 year and an increase of 55% compared to the level in 2003/04.

In terms of the average project investment, there was more consistency between agri-sectors in 2005/06 than in the previous year where there were large variations. The smallest average investment was in Viticultural investments at $30,000 while the largest was in the Other sector with $52,000.

6. Companies

Overall, there were 32 companies that had investment products available in both 2004/05 and 2005/06. Of these, 19 companies (60%) did better in 2005/06 than in 2004/05 in terms of the amount of capital they raised, while 13 companies (40%) raised less capital than they did last year (Figure 8).

The outliers to the far right of the chart (Figure 8) that had very substantial increases of capital raised tended to be newer projects that raised only a very small amount in 2004/05 and so the increase to 2005/06 was relatively large and off a low base.

A measure of how successful the year was for many products is a comparison between the actual money each raised against their initial targets. AAG has estimated from the public investment documents and other information available from the product managers that there was approximately $1,337 million targeted to be raised in 2005/06.

Given that overall the industry raised $1,141 million, the industry as a whole raised approximately 17% less than its initial target subscriptions.

Many projects, however, allow for over-subscriptions to occur and understate the desired level of sales knowing that they are likely to raise more capital than stated and therefore show sales results better than their stated targets. We also note that not all projects publicly state a target.

Compared to 2004/05 where 58% of projects achieved better than their stated targets, in 2005/06 only 38% were able to equal or better the stated targets for capital raised.

In 2005/06, 61% of projects achieved better than 70% of stated targets compared to the previous year when 71% of projects achieved better than 70% of stated targets. This suggests that it was a tougher year for capital raising in 2005/06 than in 2004/05.

Of the 39 product managers that had projects available for investment in 2005/06, 9 of these were part of ASX-listed companies. These included:

- Commonwealth Bank of Australia (CBA);
- Forest Enterprises Australia Ltd (FEA);
- Great Southern Plantations Ltd (GTP);
- Gunns Ltd (GNS);
- Integrated Tree Cropping Ltd (ITC), soon to be part of Futuris Corporation Ltd (FCL);
- Macquarie Bank Ltd (MLB);
- TFS Corporation Ltd (TFC);
- Timbercorp Ltd (TIM); and
- Willmott Forests Ltd (WFL).
All but CBA released new products in 2005/06, with CBA’s 2004/05 product available in the first part of 2005/06.

Table 2 outlines the collective results for the ASX listed sector compared to the un-listed companies.

<table>
<thead>
<tr>
<th>Companies</th>
<th>Projects</th>
<th>Capital</th>
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<tbody>
<tr>
<td>ASX-Listed Companies</td>
<td>9 (23%)</td>
<td>24 (35%)</td>
</tr>
<tr>
<td>Non-Listed Companies</td>
<td>30 (77%)</td>
<td>45 (65%)</td>
</tr>
</tbody>
</table>

Please note: we have not included a dollar figure for the capital raised for confidentiality reasons, and have included an approximate percentage figure for capital raised.

Clearly, the listed companies dominated the sector in 2005/06 in terms of dollars raised. Whilst they represented only 23% of the companies operating and 35% of projects, they raised approximately 80% of the capital (Table 2).

7. MIS and the Equities

For some time we have suspected that the sales of MIS investment products have been linked with the performance of the ASX. Given that MIS are simply another class of product available for investment it would seem logical that MIS sales would move in line with investments in other products, such as listed equities.

We used the returns from the All Ordinaries Accumulation Index as a measure of performance and when sales of MIS products is plotted against returns from the All Ordinaries, it is clear that when there are strong investment levels and returns from the ASX, MIS sales follow suit (Figure 10).

To find out the extent of association between the two we used correlation analysis.

A correlation value of 1 demonstrates that two particular asset classes are exactly linked – i.e. levels of each move exactly together – and a value of close to 1 means a strong correlation.

Low correlation between two assets means that the extent of changes in each is weakly related.

A positive correlation value means that when levels (i.e. returns or investment levels) for one asset class increases, levels for the other also tend to increase, while a negative correlation value means that when levels for one asset class increase, levels for the other tend to decrease.

Table 3 outlines the correlation values for historical MIS sales and the returns from the All Ordinaries Price and Accumulation (Total Returns) Indices.

<table>
<thead>
<tr>
<th>MIS Sales</th>
<th>AllOrd (P)</th>
<th>AllOrd (A)</th>
</tr>
</thead>
<tbody>
<tr>
<td>AllOrd (P)</td>
<td>1</td>
<td>AllOrd (A)</td>
</tr>
<tr>
<td>AllOrd (A)</td>
<td>+0.94</td>
<td>MIS Sales</td>
</tr>
<tr>
<td>MIS Sales</td>
<td>+0.82</td>
<td>+0.90</td>
</tr>
</tbody>
</table>

AllOrd (P) = All Ordinaries Price Index,
AllOrd (A) = All Ordinaries Accumulation Index

Clearly, there is a very strong relationship between the All Ordinaries and MIS Sales. The analysis shows that approximately 90% of the changes in MIS sales from one year to the next may be explained by the returns in the All Ordinaries. That is, it appears that investment in the MIS industry follows the general listed equity cycles.

Historically, the MIS sales in the MIS industry have been impacted by outside noise, such as the ATO crack down in 2001. This noise, explains the other 10% of the changes.

As we have said, we have used the All Ordinaries Index as a measure of performance of the general economy. So, when the general economy is performing well sales in MIS products are strong. Therefore, we suggest that investment in MIS is based along similar lines as investment decisions for other investment classes.
8. Location of Projects

Based on the location of the projects, Victoria and Western Australia receive 25% and 22% of the capital respectively (Figure 11).

![Figure 11 Percentage of agribusiness projects directed into each Australian state and territory in 2005/06, by capital raised (note: figures have been rounded).]

Whilst South Australia receives the least amount of capital, it still receives approximately $100 million, which is not an insignificant amount (Figure 11). This would likely rival any other agribusiness development in this state.

While non-timber companies will know exactly the area and location of their areas to be developed, timber product managers have 12-months to find and plant the land for their projects and so have provided an estimate of the areas only. Using these estimates, on the basis of area to be developed as a result of the 2005/06 capital raising year, Western Australia clearly wins with 40% of the area, while South Australia will have the least amount of development at 5% of the total or around 6,200 ha, which again, is not an insignificant area.

![Figure 12 Percentage of agribusiness projects directed into each Australian state and territory in 2005/06, by area.]

9. Revenue, Tax and Finance

Figure 13 illustrates the amount of capital raised in each year of our survey and the amount of tax refunded to investors in the same year.

![Figure 13 Approximate tax refund to investors compared to the amount outlaid on projects in 2005/06.]

Of the $1,141 million raised in 2005/06, 92% was deductible in the same year and assuming a 48.5% tax rate, this means that $510 million or 45% of the capital raised will return to investors as a taxation refund.

In reality, not all investors will be on the highest marginal tax rate of 48.5% so the figure refunded to investors will most likely be less than $510 million.

By comparison, AAG estimates that in current dollar terms (excluding any price or cost inflation) 2005/06 projects will produce $5.5 billion in farm gate revenue over the lives of the projects (Figure 14). This is a 4.8 times multiple.

![Figure 14 Estimated gross revenue for investors from sale of the crop by industry (note figures are gross income after harvesting costs but before any management fees).]
Over the last five years of project sales we estimate that the farm gate income will be a massive $16.4 billion.

Victoria will receive the bulk of the farm gate income at $2.12 billion or 39% of the total generated (Figure 15).

![Figure 15 Estimated gross revenue for investors from sale of the crop by state (note figures are gross income after harvesting costs but before any management fees).](image)

Allowing for annual management, lease and crop marketing fees, we estimate that net income to investors would total approximately $3.3 billion. Investors will pay tax on this net income. Following the recent changes in the top marginal tax rate to 46.5%, the amount of tax likely to be paid to the Government on the net project income is approximately $1.5 billion, which is 3 times the tax deducted in 2005/06. In addition to this, the product managers will have to pay tax at 30% on the management, lease and crop marketing fees. Also, there will be tax paid on salaries and wages which will grow significantly as these projects development. Pay-roll tax and very significant amounts of GST will also be paid to the Government and when combined with the tax an net crop income this industry contributes tax at substantially greater than 3 times the tax deducted upfront.

The industry employs more than 1,700 people directly and a further 7,000 people on a contract basis. Close to 400 jobs have been created as a result of the 2005/06 projects.

Approximately 72% of the investment dollars was geared through the finance arrangements available to Investors through the investment offerings while 69% of investors geared their investment (Table 4).

![Table 4 Financing of investments](table)

The difference between these two figures suggests that those gearing/financing their investment invested more than those paying cash upfront.

The MIS industry is a very significant one when you consider that project investors over the past years in just the listed companies detailed in Section 6 total over 75,000 people. These companies also currently have approximately in excess of 43,000 shareholders. These figures would climb significantly higher when the unlisted companies are included.

### 10. Areas to be Established

The main outcome of the capital raising from 2005/06 will be the significant amounts of land that will be developed to agribusiness crops. Approximately 84,300 ha of Timber plantations will be established within the next 12 months (Figure 16). This is a decline of 18% in the planting rate from the 2004/05 year.

Timber crops are significantly more extensive than almost all other crops, hence the substantially greater areas that will be established to Timber. Approximately 600 ha of vineyards will be established, 1,500 ha of olive groves and 5,400 of other horticultural crops (Figure 16) including around 4,000 ha of almonds orchards. Approximately 38,000 ha of grain crops will also be established.

![Figure 16 Areas that will be established resulting from 2005/06 capital raising season.](image)
The balance of the 2005/06 Timber plantations will be established for longer rotation sawn wood products such as pine and eucalypt sawlog (11,500 ha or 14%) and paulownia, teak, sandalwood, mahogany and oak (4,200 ha or 5%).

Figure 17 Areas that will be established resulting from 2005/06 capital raising season.

11. References

1. ABARE 2005, Economic Overview, Australian Commodities, vol 12, no 1, pp 5 – 18

12. AAG Profile and Contact Details

Australian Agribusiness Group (AAG) was formed in 1997. It provides agribusiness, research, investment and management skills to smart agribusinesses.

AAG is the market leader in research into the agri MIS sector. In alliance with Ernst & Young, it provides detailed research and rates product offerings and supports the sector with a range of decision making tools. Its research reaches over 140 financial planning groups, covering some 9,000 financial planners. AAG’s ratings are also distributed by Standard & Poor’s.

AAG provides research to other high growth agribusinesses, manages Stocklease Pty Ltd, provides investment and management services and operates a national consulting practice.

AAG also produces the Agri Index, a measure of the relative performance of ASX to listed agribusiness.

For more information about the AAG please visit www.ausagrigroup.com.au.