

DISCONTINUING DISCOUNTING?

At the Institute Annual General Meeting in May it was refreshing to hear the then Director of the Institute of Economic Research (Inc.), Brian Easton, admitting that "the time dimension creates very great problems in economics, and the good economists always approach time-dependent problems with the greatest respect".

For foresters, such an observation is very pertinent, for many have been uneasy about the uncritical use of discounting which they felt that economists were insisting upon. The effects of discounting at a 10% real rate, as the N.Z. Forest Service has practised, has had profound effects on forestry. It has virtually confined production plantation forestry to radiata pine grown on short rotations. It has also had a large influence on tending practices, land acquisition and restricted our thinking and management of indigenous species. The use of short rotations has important consequential effects on intrinsic wood properties in species like radiata pine, and influences the timing and nature of industrial expansion. It also influences stumpage expectations when the wood is sold, and is often involved in valuation exercises (see review by B. Everts, p. 30).

But what was the rationale behind the choice of a real 10% discount rate used by State? John Purey-Cust, our former editor, wrote to the Treasury seeking the information under the Official Information Act. The reply contained a copy of a review paper on the public service discount rate prepared by Dr. B.D. Wilkinson in 1981. This review considered seven suggested methods of deriving a suitable rate, all of which were based on economic criteria. Some of the more important points made were:

- The common assumption that the Public Service discount rate should be the same as the social rate of time preference (i.e. the marginal productivity of capital in the private sector) "is not necessarily optimal".
- "It is reasonably safe to conclude that the rate of return on capital at the margin in the private sector is at least 10%".
- "The major conclusion therefore is that determining the Public Service discount rate is inevitably a political/democratic decision which must involve weighing of social opportunity cost, rate of time preference, cost

of overseas and internal borrowing issues. It is impossible to determine the optimal rate independently of a knowledge of the implications of that rate for the volume of capital expenditures and taxation. In fact causation primarily runs in the other direction. During the course of the budgetary process Governments determine the desired rate of public investment taking all relevant rates of return, internal/external balance and tax considerations into account. Given the menu of investment opportunities this quantity decision determines the cut-off Public Service discount rate."

In this issue Jeanette Fitzsimons argues for a much wider perspective and the use of different criteria for decision making (see page 22).

If her arguments are heeded they

could change the direction of forestry. Her wider perspective makes the Treasury report on Public Service discount rates appear rather narrow. Also recently we have seen the larger forestry companies employing discount rates substantially under the 10% criteria (see page 23). Will Government moves to create State Corporations, which will be more subject to market forces and will be funded independent of taxation, have repercussions on the use of discounting? Will the Government now accept wider criteria for funding the new departments without trading functions? Perhaps, as Brian Easton commented at our Annual General Meeting, whereas discounting methods have dominated in recent years, they may not in the future.

Don Mead,
EDITOR

NZ Institute of Foresters

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"We trained hard. But it seemed that every time we were beginning to form up into teams we would be reorganised. I was to learn later in life that we tend to meet any new situation by reorganising; and a wonderful method it can be for creating the illusion of progress while producing confusion, inefficiency and demoralization."

— Petronius Arbiter,
210 B.C.

I am grateful to Mr A. L. Poole for drawing my attention to this quotation. I believe it is as appropriate today as it was in 210 B.C.

The Editor of Australian Forestry in his comments on the 1985 Conference in Hobart said of the keynote speech that it had "a pronounced impact on the Conference and was the basis of much discussion throughout the week".

Catherine West, the keynote speaker, said that the then new New Zealand Government appeared to her to be committed to conservation, and to be engaged in the potentially dangerous debate about the possible administrative separation of development and conservation. This suggestion, she said, is the antithesis of professional forestry, which has to be concerned with the balance

between these two related areas. Good forestry, like good politics, she claimed, is a matter of time. Preservationists have, in her opinion, no interest in timing, as they desire only to preserve what is. Professional foresters, on the other hand, are concerned to balance what is with what needs to be. Foresters, she said, combine a desire to minimise damage and maximise community opportunity and benefit.

Since the Hobart Conference we have seen massive changes within New Zealand to the administration of public forests. There are also proposed fiscal changes which, if adopted, will have a profound effect on the management of privately owned forests. Over the past 12 months, the New Zealand Institute of Foresters has, at every opportunity, been active in commenting loudly and strongly to Government on these proposed changes.

The original direction Government took seemed to be towards the fragmentation of State forest administration into the artificially separate conservation and production components. This appeared to most responsible land managers to be a total Government sell-

out of the environment to the preservationist lobbies. The path beaten to Government's door by the Institute and others was not as effective as that chosen by the preservationists who had had years of active campaigning behind them, and were initially very much in command of the situation.

The Institute felt compelled to continue to comment despite its apparent lack of success. Government finally made environmental administrative changes which run counter to the direction that the Institute would have chosen. The decisions Government have made to reorganize the State's environmental management will, they believe, result in more transparent departmental accountability. The institute was initially bitterly opposed to the concept of the reorganization on the grounds that it is ridiculous to separate conservation from development and that the environment must be managed on multi-purpose lines.

After spending the last 12 months actively studying and commenting on Government's moves, my present thoughts on the administrative changes are:

1. The Environmental Commissioner and the Ministry of the Environment are positive steps in the regulation of environmental administration. Both these agencies should ensure that environmental issues are exposed and reported. Provided they function in a balanced way, they will keep environmental administration pure and will comment on transgressions by all parties including politicians.
2. Department of Conservation is an attempt by Government to manage conservation areas by one agency. The final environmental purity of the department has yet to be determined. There are some who would like to see it administered on strictly preservationist lines, while others, and I include myself among those, applaud the recent suggestions that the department will have a productive role in indigenous forests. I strongly believe that the absurdity of totally separating conservation from production must be avoided if the environment is to be wisely managed. The multi-purpose use of the environment must be preserved in a balanced state if environmental evolution is to continue. The Department of Conservation with its heavy environmentalist overtones will, I believe, be less susceptible to external pressures than the two departments from whom it was wrested. It must be continually borne in mind that Government, in its quest for transparency, has created an en-

vironmental management department which will be funded directly by Treasury. Sensitive portions of the environment will effectively be in the hands of the Treasury Ministers.

3. The proposed Forestry Corporation has two courses to follow. It can either:
 - (a) become lean, mean and strictly commercial. If this is the case I believe the potential does exist for the eventual take-over of large portions of the sector by a successful Corporation. It must be remembered that even a strictly commercial forestry venture, if it is to follow proper forestry practice, must make allowance for non commercial environmental aspects such as erosion control, visual impact, downstream values and so on. or
 - (b) accept the position of manager of the State's exotic forests and take over that portion of the Forest Service, warts and all. If this is the case, the management of the State's exotic resource should not prove a threat to the forestry sector. It will, however, have been an expensive exercise to increase the transparency of the State's commercial operations.
4. The Ministry of Forestry is to be the promoter of the national interest through forestry and wood-based industries. It effectively takes over those portions of the Forest Service not grafted onto the Department of Conservation or hived off to the Forestry Corporation. Government are to be congratulated on their wisdom for retaining an independent and stand-alone servicing and regulatory

agency. The forestry sector needs a governmental point of focus. The Ministry of Forestry will provide this.

5. No discussion on Government's revolutionary changes over the last 12 months would be complete without consideration of the proposed fiscal changes outlined in the Minister of Finance's Consultative Document on Primary Sector taxation. Despite the paper's protestations to the contrary, I firmly believe that the proposed tax treatment of forest investment will be a direct disincentive to investment in future forestry planting. The proposed tax regime treats forest investment initially on a capital basis; at time of logging a forest is treated as a trading item then at time of re-establishment forest investment is again treated as capital. This, I believe, is effectively a double taxation and, as such, will in time reduce the resource base of the forest industry.

The last 12 months have been witness to environmental revolution. As an Institute we have resolutely pursued the ideals set out in the Constitution. We have promoted the best use of New Zealand's resources. We have encouraged the wise use of forests and forest land, and we have continued to further the interests of the profession of forestry. Such ideals must continue. It is imperative that as a profession foresters continue to play an increasingly prominent part in land use and management matters at both political and public levels. The revolutionary fervour that abounds must be encouraged to evolve into balanced resource management.

**W.P. Studholme,
President**

NEW COUNCIL

Following the tragic death of the newly elected President of the Institute, Curt Gleason, Council confirmed on July 31, 1986 that the following will hold office for a two-year period:

President: Peter Thode

Vice President: Peter Berg

Secretary: John Holloway

Treasurer: John Valentine

Other Councillors: Harry Bunn, Lisa Crozier, Ben Everts, John Glead, Lindsay Vaughan.

Consultant Committee: Hamish Levack

Journal Editor: Don Mead.

For our obituary of Curt Gleason, see page 26.