The events of 1987
Corporatising and privatising the state's forests

Peter Berg

The history of forestry in this country has for more than a 150 years been entwined with government policies and the nation's politics. During the first decades of European colonisation the forest's place was a matter of scant regard, with successive 19th century governments promoting settlement as a matter of priority.

By the turn of the century, the success of this philosophy was creating some concern. Forests and their products played unique roles in both the social and economic development of the country. Their apparent decline resulted in the realisation that this essential ingredient of the nation's cultural and commercial heritage needed to be maintained.

The Royal Commission in 1913 generated much more focus on forests and wood resources. This led to the establishment of the State Forest Service in 1919 and promoted greater interest in planting radiata pine among a wide range of other matters.

Over the next 60 years or so the Forest Service and plantation forestry in New Zealand flourished. It was the product of a rich mix of economic and ideological vision, pragmatism, team-work and a certain amount of good luck. Government land use, economic development, employment and other policies helped, so much so that the department was the largest owner of commercial forests in the country and also has a major stake in the wood processing industry. It is therefore no surprise that the major restructuring of the Forest Service in 1987, and the story of the short-lived New Zealand Forestry Corporation, had as much to do with politics as with trees and timber.

Reasons for change

While the capability of the extensive forests established by the department was recognised at a reasonably early date, it was notable that matters such as commercial return were not always the main reasons behind the forest planting and management programme. Other factors, such as soil conservation, employment and regional wood supply often rated higher in decisions to locate and plant forests.

Although different policies predominated in different regions there is little doubt that Forest Service planting programmes were sometimes opportunistic, designed to fit circumstances which would allow further planting to take place. For example, employment-related planting programmes were a favourite. This opportunism probably contributed to situations where the investment strategy could be, and was, challenged.

Commercial potential

By the 1960s the success of the Kawerau and Kinleith pulp and paper developments, and the switch to plantation-grown timber in domestic and commercial construction, were demonstrating the commercial value of the forests. In 1969 a forestry development conference, one of the sector groups set up under the broader national development conference, identified forestry as a potentially major export resource. It proposed planting and harvesting targets for both the state and private sector, and market development work that would see that potential realised.

The Forest Service was owner of well over half of the country's production forests and was therefore harvesting more than half its wood. In several regions it was the only organisation selling logs to local wood processors. In the best tradition of pork barrel politics, appeals to the Minister for wood supply and at affordable prices were often successful. The Forest Service had limited ability to influence these decisions or to impose more market-related criteria to the sales process.

Multiple use

At much the same time the Forest Service was developing environmental goals, and subsequently formed an Environmental Forestry Division, decisions which gave impetus to the separation of the department into factions and supporting a multiple use forest policy. This multiple use concept gave weight to environmental and social considerations along with commercial use of timber. The total of these values was used to justify forestry activity in situations where, on commercial grounds alone, it was unlikely to have succeeded. The department found itself with a range of criteria to satisfy, and it required staff with wider specialisations than a more pragmatic approach to commercial plantation forestry might have needed.

Environmental objectives

The Forest Service had taken the lead in setting environmental objectives. However, its approach to managing forests, especially indigenous forests, was coloured by an understanding of the regenerative and silvicultural capacity of its forests not always shared or appreciated by members of the wider community. A conservation movement, buoyed by a successful 'Save Manapouri' campaign, which ultimately stopped the lake level being raised to support a major hydro-power scheme, next targeted Forest Service proposals to harvest West Coast beech forests.

This confrontation lasted more than a decade and also spread to other areas where Forest Service management of native forest was similarly viewed with suspicion, and where equally heated campaigns to halt this activity ensued. In native forests, at least, conservationists rejected the philosophy of multiple use, concluding that it was not possible to reconcile commitments to production forestry with recreational use and the protection of bio-diversity.

Special employment

Of course politicians seldom helped Forest Service attempts to determine a more rational strategy. For example, in 1972, just three years after the first forestry development conference, the government of the day was proposing soft employment policies to be implemented by the Forest Service. These were special winter and periodic employment planting programmes targeting localities where lack of work opportunities were a particular problem.

Ironically these special employment-related planting programmes were instrumental in the department meeting and exceeding its planting targets, although subsequent events were to lead to pointed questioning about the location and commercial worth of this activity. In 1984, it was revealed that at the then National government's insistence it was proposed to open up and harvest areas at Patunamu Forest, south of Gisborne, for supply to a new mill. It was to be at a stumpage price which would not even cover the cost of providing the road.

The Forest Service was not silent on these matters. As early as the 1970s, Priestley Thomson, in his capacity as head of the department, challenged the government over its employment policies. He felt they were distracting the Forest Service from the clear commercial objectives established at the forestry development conference and associated with its exotic plantations. At the next forestry development conference in 1974, the department released a new indigenous forest policy designed to clarify where and under what circumstances wood production activity was permitted. However, it did little to allay conservationist concerns, while staff inside the Forest Service also grappled with its implementation.

Financial management

The influence of the Treasury, and its concerns about financial management in the process leading up to the division of the Forest Service in 1987, is not always well understood. During the 1970s the Audit Office, which had oversight and reported on the bureaucracy's spending of taxpayer's money, was beginning to question the financial competence of departments.

A 1978 report, which reviewed at least 15 departments, concluded that there was little coherence between departmental aims and associated financial reporting. Quick to respond, the Forest Service set up a financial reporting review team. However, without a matching reform of the roles and accountabilities within the organisation, this was never likely to be successful. As the then head of department, Andy Kirkland, noted: 'later, when the goal of running a successful business was established (the Forestry Corporation), the relevant accounting systems quickly fell into place.'

In 1980, the influential Public Expenditure Committee of Parliament also took a considered look at the Forest Service. It concluded that if it was to contribute to both export and domestic economies, it needed to be freed of rigid administrative controls which reduced market flexibility and trading efficiencies: 'the majority of the committee is of the opinion that a limited liability company would best suit the needs of the Forest Service.' At yet another forestry development conference in 1981, National Party back-bencher Ian McLean proposed the separation of the commercial forests from the rest of the Forest Service.

While the idea was not actively pursued by either the department or the government, it encouraged the conservation movement to forge closer political links, particularly with the Labour opposition. Policies around stopping harvesting in virgin native forest and greater legal protection for all native forest emerged, and were important aspects of Labour Party policy when the snap election was held in 1984.

At the time, the Forest Service chose to shelter behind the multiple-use philosophy enshrined in a 1974 amendment to the Forests Act. However, in 1989 Andy Kirkland, then Managing Director of the Forestry Corporation, suggested to the Commonwealth Forestry Conference in Rotorua that adherence to multiple use had probably done forestry a disservice and had undoubtedly contributed to the restructuring put in place in New Zealand.

The decision to change

It is now a matter of record that when the Labour Government came to power in 1984 New Zealand was effectively bankrupt. Funds continued to pour out of the country and it took an immediate 20 per cent devaluation of the currency, and other measures, to stem the outflow. The new Minister of Finance, Roger Douglas, had spent years analysing the problems of the New Zealand economy, and with the support of his colleagues set about making the changes he considered necessary. Apart from an over-valued exchange rate, distortions in the economy due to subsidies were identified.

In the forestry sector, Tasman Pulp and Paper Ltd got a mention. Douglas' 1980 booklet *There's got to be a better way* suggested that the government subsidised Tasman to the tune of $40 million in 1979 and 1980. This was a $49 subsidy for every cubic metre of saw logs the company acquired. This was based on a stumpage payment of $3.04 to the Forest Service and an available export price of $52 for the same material. When the new government produced its first budget forestry investment, concessions had been removed and state wood prices were to reflect the cost of supply.

The next step, to corporatise parts of the public sector, had also been signalled in the booklet where Douglas advocated turning railways into a corporation, the clear implication being that the state was not competent to run profitable businesses. His associate, Minister Richard Prebble, agreed that government departments were often 'out of control'. He also said: 'Efforts to improve Forest Service accounting had been attempted for years but became bogged down – because successive governments failed to provide any clear objectives for the department.'

Treasury agreed, although the corporation model was not then identified by them as the solution. Minister Douglas and his two Associate Ministers, Prebble and David Caygill, considered the solution was to be found in making the state enterprises act 'more like the private sector'. Prebble is reported as saying that at that time there was no discussion of privatisation, just a desire to make the state sector more efficient.

On 16 September 1985, Cabinet decided to establish commercial forestry and lands agencies with a separate conservation department. The nature of the corporation, or indeed just what assets it would control, were yet to be resolved. However, once determined, the new agencies were to be in place and operating as soon as practical – subsequent decisions meant that this would be 1 April 1987. Not surprisingly the proposed changes met with some resistance from the bureaucracy and the state sector unions, although this was somewhat muted by the acceptance in the wider community that such moves were necessary.

Policies for direction

In December 1987, Douglas produced a principles paper setting out policies for state owned enterprises which gave greater direction to the restructuring process including –

- Responsibility for non-commercial functions was to be separated from major trading enterprises
- A principal objective would be to run state enterprises as successful businesses
- Managers would agree performance objectives and would be accountable for their performance
- Barriers to performance would as far as possible be removed so performance could be judged by commercial criteria
- Each state enterprise would be restructured according to its commercial objectives under the guidance of boards generally appointed from the private sector.

Following on from this, later in December Andy Kirkland flew to Auckland to meet with two well-known private enterprise exponents in the persons of John Fernyhough and Alan Gibbs. Both of them were to be invited to set up and be on the establishment board of the proposed Forestry Corporation. After a day or so to think it over, both agreed to participate.

On 19 February 1988 this Board was appointed, and its first requirement was a report on the establishment of the proposed corporation. Gibbs immediately sat down and produced the first draft 'over a weekend'. It was provided to government on 15 May, and gave clear and quite definite views on market orientation, structure and employment policies which later set the bench-mark for other state owned enterprises.

Told to get on with it by Douglas, the Board and a small but dedicated group of staff set about implementing the plan, while the government for its part addressed an array of legal and other issues. The State Owned Enterprises Act became law in December 1988. The establishment unit of the corporation produced the proposed staffing structure and in November was inviting applications for positions in the new organisation.

Spooked by the sudden appearance of a new heavyweight competitor operating across the forestry value chain, the sawmillers and other wood processors drew up plans to create a $250,000 fighting fund to oppose its establishment. On 1 April 1988, hundreds of former employees became contractors overnight, often using machinery and equipment belonging to the former Forest Service but now acquired as part of an arrangement to provide services for the future.

Of more than 7,000 former employees, around 550 were offered roles as corporation staff, while another thousand or so continued in the businesses now servicing the new organisation. About 700 wage workers were employed in the sawmills.

Maximising returns

The corporation itself operated through separate forestry and wood processing arms, managed so that financial performance in each case was easily seen. In the entire 68 years it had existed, and despite its immense and continually growing value, the Forest Service had never reported a trading surplus. In its first two years the corporation generated cash surpluses of $174 million, and as its confidence grew was forecasting even better returns.

Its commercial focus was very much on maximising return from existing forests and growing these as efficiently as possible. 'Optimising performance along the value chain' was the catch-phrase of the day and non-commercial assets were identified for disposal or other action as appropriate. The native forests of the West Coast identified for wood production as part of the West Coast Accord were somewhat reluctantly included. This was not because of any doubt about the ability to manage these on a sustainable basis in perpetuity, but rather because of strong doubt about the commitment of the parties to the Accord.


Kaingaroa Forest is where large-scale state forestry began


Jim Nicholson and Geoff Chavasse discuss the quality of kauri seedlings at Sweetwater Nursery in the 1970s

Privatisation

Although the Labour Government won a second term in 1987, the euphoria of 1984 had largely dissipated. There was increasing pressure from among its own ranks to conclude the asset sales programme, especially from the unions whose concerns about job losses were becoming more widely shared, and there was also equal pressure to reduce overseas debt.

There seems to have been little argument about whether to privatise the corporation at some point, both Gibbs and Kirkland agreeing it was a logical corollary of the corporatisation process. However for Kirkland, the timing and form of sale was critical, and he was anticipating adequate time to get things into shape. For others, including Douglas and his Treasury advisors, it was more a question about whether a sale of forest assets or a sale of the corporation, or shares in it, was preferable.

In their book *Out of the Woods* (1993), Birchfield and Grant say that corporation Chairman Alan Gibbs confirmed to Douglas in early 1988 that at that time there was little or no logic to the corporation's portfolio of forests and processing activities. They also said that it would take considerable time to rationalise the business to the extent of it being a credible contender for public listing.

Privatising the forests

The wood processing industry was meanwhile pursuing its own agenda. A powerful wood processing competitor, especially one which controlled more than 50 per cent of the forest resource, was a dangerous neighbour and needed to be cut down to size.

It seems that ultimately the failure of the corporation to reach agreement with Treasury over the value of its assets was of more significance than any other factor in the decision to proceed with a sale of the forests. This, along with the need to achieve the government's economic goals and the disintegration of political unity in the Labour Party, all contributed to Treasury's support for the corporation waning. In its July 1988 budget, the government announced it would be privatising the forests. It was a bitter blow for those in the corporation, particularly Andy Kirkland who was strongly committed to the loyal and capable team he had built around him.

As General Manager of the corporation's operations, I remember that Andy needed time to reflect on the decision. He left a comprehensive delegation of his authority on my desk and simply disappeared for almost three weeks. Alan Gibbs rang a day or two later and checked I had the paperwork but offered little else. He seemed to assume I knew what was happening and requested I simply continue to report to him as Andy did.

Problematic selling

Kirkland returned, charged with the view that the best way to sell the forests to advantage was to have the corporation team, who knew them better than anyone else, manage the sale. Surprisingly Treasury agreed, and within days the corporation was once more divided, this time into management and the asset sale teams.

Selling the forests proved to be much more problematic than even the staunchest advocates had anticipated. While Treasury and the government were

The Forest Service administered rural fire protection

The work of Fenton and Sutton revolutionised silvicultural practice and was quickly adopted expecting a massive cash windfall, it soon became apparent that there were also significant caveats to the sale which had the potential to impinge heavily on the value of the assets for sale. Contractual constraints, such as the Tasman sale, which still had decades to run, and other company claims to pre-emptive rights to wood from forests as a result of the earlier establishment of wood processing facilities, generated uncertainty both about exactly what assets could be sold and their value.

More complex were iwi claims to land and forests in every part of the country. Ultimately, the sales team and Treasury negotiated a formula with Maori representatives which preserved their land claim rights while maintaining security of cutting rights for the new forest owners in the event of a successful land claim.

The sales

The Crown Forests Assets Act 1989 provided enabling legislation for the sale – purchasers would acquire the trees, buildings and other fixed assets with the land remaining in Crown ownership and leased to the forest owner via a Crown forestry licence. The licence generally provided for a 35-year rolling term until triggered by a termination notice, which in turn could only be triggered by the Waitangi Tribunal recommending return of the land to Maori ownership.

In October 1989, the sales team issued the prospectus for the sale of the forests and associated assets. The prospectus concluded that the sale would set the pattern for the future shape of the New Zealand forest industry and would also –

- Provide the opportunity for existing users of state wood to secure long-term supply and encourage further investment in processing capability
- Provide resources for new ventures in wood processing
- Encourage joint ventures between new forest owners and wood processing companies
- Allow existing wood processors to become vertically integrated
- Provide investment opportunities in forests, especially younger trees.

Tenders closed on 4 July 1990 and two bids were quickly accepted on 73,000 hectares for $364 million, while negotiations resulted in a further 174,000 hectares being sold for $663 million. In May 1992, most of the unsold forest outside the Bay of Plenty was sold to ITT Rayonier and the Bay of Plenty forests in 1996. The West Coast forests remain with the Crown, although as anticipated, indigenous production forests were 'retired' as signalled by the Labour government in its manifesto before the 1999 elections.

In the Birchfield and Grant book *Out of the Woods*, I noted that, even with the benefit of the drawn-out asset sale process, it was difficult to be precise about an appropriate value for the forests in 1987, but concluded that it was no more than $2 billion. The change in the pattern of exotic plantation forest ownership was significant, as the table below, reproduced in part from *A Century of State-Honed Enterprise* (Kirkland and Berg 1997), indicates.

Owner	October 1989 percentage	December 1996 percentage
State and Forest Service	48	1.6 retained in crown ownership
Fletcher Challenge	11.5	
Elders and NZFP	13.3	25.7
CHH	5.2	
Crown leases	3.9	22
Others	18.1	3.5
Timberlands West Coast		29.8
Ernslaw One		1.7
JNL		1.7
ITT Rayonier		3.5
Hawke's Bay Forests		6.6
Wenita Forest Products		2.2

It is, of course, a matter of history that forest ownership has continued to change as a consequence of these events and the pattern of ownership has become even more diverse with the passage of time.

Significant investment on the back of the forest sales has eventuated, including new ventures of importance in the wood products export business. Some of the new companies remain vertically integrated, at least in part, while extensive international interest in the opportunity to invest in trees is very much a core part of New Zealand plantation forest ownership. As Kirkland concluded in the final pages of *A Century of State-Honed Enterprise*:

> The State's role in commercial plantation forestry in New Zealand could, perhaps simplistically, now be seen as consisting of a single self-sacrificing mission – to act as the catalyst for a vigorous, sustainable private forestry sector capable of meeting the domestic demand for forest products and making a significant contribution to national export earnings. ... The State legacy remains abundantly apparent in the forest resources of the privatised forestry sector.

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