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Veon *Vision*

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Individual Highlights

Covid-19: Consequences for Forestry in Ireland

We are in a situation no one could have predicted as we entered 2020 and now face the global pandemic through social distancing, to initially slow the spread of the virus, and hope that a vaccine can be found in the short term. In the meantime we are finding alternative means of conducting our lives, our society and our industry sectors.

Forestry in many regions, Ireland included, was identified as an essential service. That is not to say it has been business as usual – far from it. Forestry plays a critical role in the economy and this was clearly identified from the outset as the sector was permitted to proceed under amended operational guidelines. Indeed, we are alert to one jurisdiction that initially kept the sector out of the essential services list only to have to introduce it some weeks into the crisis.

Irish timber markets were starting to experience the realities of working in a lockdown environment, and by early April many processors had adopted reduced shift patterns or site closures. With the exception of pallet wood which has seen significant price movements, Irish timber prices have fallen steadily over the past twelve months.

The most significant impact to the timber market has been in the cessation of building work, which removed saw-log demand. 80% of Irish processed timber is exported to the UK which has experienced its sharpest decline in GNP of 5.8% in March with the largest quarter-on-quarter fall since the end of 2008, during the depths of the financial crisis

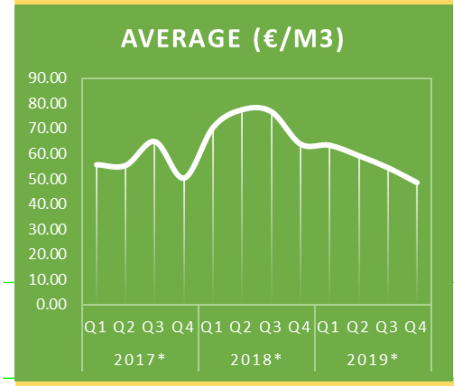
On 30th April, the Minister for Finance, Pascal Donoghue, stated that the Irish economy would shrink by 10.5% this year. Because the situation is still evolving it is not possible to predict how damaging the effects of Covid-19 will be to the Forest industry - suffice it to say they will not be positive.

Veon supports the re-envisioning of the forest industry sector to continuing research on the tree species we plant; how our forest industry produces and processes Irish timber to ensure that a greater proportion of our timber is utilised with more environmentally friendly timber framed offices, schools and homes and a greater shift to a more advanced bio-economy. Veon is committed to promoting higher end uses for timber and realising the intrinsic value, both economic and biological, of this wonderful natural resource that grows in our forests.

Veon is a member of Sustainable Nation Ireland which is focussed on positioning Ireland as a centre and world leader in sustainable business and helping in the transition to a sustainable, low-carbon economy.

Timber Price

Timber prices have continued to fall since their peak in Q2 / Q3 2018. The chart below demonstrates this fall and it is to be noted that the data ends in Q4 2019. As such, the price data has no data concerning the impact of Covid-19 as the pandemic did not emerge in this part of the world until much later.



Veon's experience of the market since the New Year is that it continued to weaken in the first months due to the combination of a regulatory and market driven crisis – on the one hand felling licences applications were stalling in the Forest Service which should have had the effect of constraining supply and improving prices. However, on the other side, there was a continuing weakness in the market due to an oversupply emanating from the continent.

Since the Covid-19 emergency lockdown, the market has been unpredictable. Sawlog, usually the most valuable product in a timber harvest, has been very slow to move while pallet, used in transport pallets, has been seen significant demand in the market. Other product types have been moving.

Overall, the sector has been very fortunate that it remains in the essential services category and has therefore remained open for business, but only time will tell what the long-term impact on timber prices will be.

Regulatory Crisis at the Forest Service

The current regulatory and licencing system is a major obstacle facing the industry in Ireland and needs to be completely overhauled and streamlined as a matter of urgency to prevent imminent industry collapse.

Ireland already intends to increase its level of forestry by 8,000 hectares a year. This is vital in terms of achieving our carbon reduction goals of 7% per annum. This is unlikely to be possible under the current regulatory and licencing system which presided over the worst year for planting nationally since 1949 with less than 3,000 hectares planted in 2019 – and 2020 may even be worse.

"...licencing system is a major obstacle... and needs to be completely overhauled ..."

The current licencing problem has been caused by the introduction of new Appropriate Assessment procedures for screening forestry projects, following the EU Habitats and Birds Directives. The Department of Agriculture, Food and the Marine has introduced a rigorous screening system, but this system is not currently functioning as required.

The current rate of approvals of forestry projects is 50% of the required rate which is significantly impacting the industry and threatening small businesses and jobs. The rate of processing appeals by the Forestry Appeals Committee (FAC) is also at only 50% of the required rate, and there is an ever-growing backlog of forestry appeals with projects being delayed for months and years. The FAC appeals process had also allowed forest objectors to freely submit blanket objections to most forestry projects, with 60,000 tonnes of timber stalled in one week alone in April. Ireland's forestry industry is in a crisis which could see the country's sawmills run out of wood by mid-June.

According to Mark McAuley of IBEC's Forest Industries Ireland "We can't get the trees planted and we can't harvest the timber".

The licencing system needs to balance community, environmental, economic and commercial concerns and needs to be adequately resourced. Environmental responsibility and a healthy forest industry can go hand-in-hand if the system is robust and properly implemented.

In order for the industry to aid in the green economic recovery, for jobs to be maintained and for climate change goals to be achieved, the licencing system needs to be fundamentally changed.

Collapse in New Planting

Proof of the Department of Agriculture Food and the Marine's continuing abject failure to oversee the forestry sector in Ireland was reported in media outlets in early June suggesting just 254 hectares of forestry has been planted so far this year. Official statistics from the Forest Service contradict this and report 883ha of afforestation grants being paid up to the end of April. However, some of these lands were inevitably planted in late 2019, so the accurate figure lies somewhere in between. Adding to these dire figures is the reported 23% reduction in planting approvals issued up to the end of April 2020.

The Government's plan to plant 8,000 hectares per year to offset agricultural sector emissions is a pipe dream. 2019 saw the lowest level of new forest planting in Ireland over the last 70 years which again calls the DAFM's commitment to the sector into question and raises significant questions about levels of competence within the Department itself.

The latest statistics demonstrate a sector in deep crisis. The organisations working within it, which includes the Forest Service itself, are configured to oversee the planting of up to 20,000ha of forestry per annum while it currently has a modest 8,000ha annual target.

The failure rests firmly within the Department. It is incapable of processing the necessary licence applications within a legislative environment that they themselves established through the Forestry Act 2014.

Enough. Ireland requires a functioning licencing system for all forms of forest licensing. This licensing system must be properly scoped and defined, including strict timeframes, so that industry can understand and deliver on its commitments to forest owners, and enable timber processors plan for their business.

Forestry in the Climate Debate

The first three months of this year were the warmest in 100 years. According to the European Copernicus service, last year was already the hottest on record in Europe, with the annual average temperature 1.24 degrees above the average for the years 1981 to 2010. 11 of the 12 warmest years in Europe were between 2000 and 2019. Scientists at the EU's Joint Research Centre forecast increasingly more severe drought in southern Europe likely to become more frequent throughout the rest of the century. Furthermore, persistent drought across swathes of Europe could now become the new normal weather pattern.

The research comes amid warnings that a catastrophic lack of rain this year in parts of Europe is again threatening farmers recovering from the hottest year on record. European mean temperatures in the last five years increased by 2 degrees Celsius (3.6 degrees Fahrenheit) above averages recorded in the second half of the 19th century, according to Copernicus.

Bark beetle infestation across central Europe's spruce forests continues to pose an additional significant threat to forests and ultimately to timber markets. Recent mass bark beetle outbreaks and their widening geographic spread have many countries on high alert to mitigate its ecological and economic impact.

Bark beetles are a natural part of a conifer forest's life cycle, but the scale and intensity in population growth over the past two decades is of enormous and alarming concern. Rising temperatures are preventing widespread winter die-back of beetle larvae, while also enhancing the beetles' potency. The beetles are expanding into new territory, hatching earlier and reproducing more frequently. Along with other more widely reported events such as melting icecaps, this escalation of beetle damage is the face of climate change.

"European mean temperatures in the last five years increased by 2 degrees Celsius…"

While impacted regions work their way through this crisis, forestry is also being widely recognised for the carbon storage capabilities that it represents during a time of climate crisis. Forests are carbon sinks – their lifecycle involves the absorption of carbon. However, to simply grow a forest and leave it unchanged upon maturity is to miss the full extent of the carbon opportunity.

Growing forests captures carbon. To truly maximise the carbon storage opportunity, mature trees must be removed from the forest and put into storage. What is storage? It is achieved by converting the timber into buildings, furniture and other products that have long lifespans. The carbon in the wood used in the construction of these products is then stored away.

Of course, there is then the issue of the cut down trees. This is the point at which the carbon opportunity expands. So long as the forest is promptly replanted, then the "new" forest grows and absorbs more carbon adding to that from the first forest rotation that is now stored within buildings or other products.

Harvesting of forests plays a vital role in the long-term storage of carbon so long as the resultant timber goes into long-life products. Irish timber is heavily utilised in the construction sector and so the harvested timber along with its stored carbon is heading into long term storage. As with all processes, there is some waste material and this heads into a combination of panel boards such as MDF, which is also a long-life product, while some goes into biomass material to offset the use of hydrocarbons. While this final element of the tree's carbon is released quickly, it is a relatively small percentage of the overall carbon in the tree and occurs as a substitute of the CO_2 that would be released from hydrocarbon fuels.

Significant work is underway around Ireland to develop higher and better uses for the timber produced in Irish forests. A leading example is the work being carried out in NUI Galway where significant work surrounding the use of cross laminate timber ("CLT") in buildings is being carried out. CLT can dramatically improve the strength characteristics of timber and brings with it a range of benefits. It is used in many other countries' construction sectors and Ireland must follow suit.

The use of CLT will expand the utilisation of timber in long-life construction projects. This will deepen the available pool of potential carbon storage sites and improve Ireland's capacity to positively contribute to solving the continuing climate crisis. Better still, it will do so in a way that also supports continued economic expansion. A true win-win scenario and one that is available now.

Investment Outlook

In light of the climate risks previously outlined, Veon recommends a long-term hold position for forestry assets, preferably until the mid to late 2030s at least.

We all recognise the need to plant more forests which are an absolute necessity for environmental, social and economic reasons.

Forestry is critical to enhancing wildlife habitats and biodiversity. Along with the valuable role commercial tree plantations play in combatting climate change, forests not only act as a great 'store' for carbon, but well managed and productive forests also 'sink' additional carbon as they grow. Our forests are so much more than just another "asset class" - they provide real social environmental and economic benefits.

Brexit

As the UK government blusters its way towards its 31st December 2020 transition deadline it looks increasingly likely that the UK is steeling itself for a hard Brexit.

EU officials recently expressed their annoyance and frustration that Britain had not yet even presented a position paper, while insisting that agreement had to be concluded in just a few rounds of week-long talks.

The penultimate round of talks before June takes place later this month, when London has said it will decide whether to abandon talks and instead prepare to switch to default WTO trade rules in January, which Germany's main business lobby has predicted would be an economic disaster.

Irish timber processors will inevitably then have to face increased bureaucracy and border controls in the event that a hard border is created on the island with knock-on effects for Irish forest owners.

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Value in Forestry

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Impact Investing

Forest owners produce a natural commodity in timber, one of the most important raw materials in modern society. As discussed earlier, the timber is also a store of carbon while the creation and maintenance of such forests requires a skilled workforce. There is a further benefit to commercial forests. Through their very existence they take the pressure off the remaining natural forests around the world – forests that must be protected.

Countries with developed, productive and well-regulated commercial forestry sectors also tend to have well protected natural forests since their timber requirements are satisfied by the timber being produced more efficiently and effectively by the commercial forests.

Veon is proud to work with various partners in a number of jurisdictions to develop both commercial forest portfolios and also to protect and rehabilitate natural forests. Through engagement with certifying bodies, Veon is working to further expand such activities.

It is noteworthy that many clients, especially corporate clients, are moving away from pure profit driven models and now demand visibility of what other benefits accrue from the forest portfolio.

By measuring the social, environmental and economic returns, Veon can identify to clients the wide benefits that are being delivered to them and by them as a result of their participation in this important asset class.

Such projects demonstrate how the corporate and high networth communities can work to deliver for both their own needs and for the wider community around them and we proudly work alongside such clients

Veon's Services

- ***Forestry Consultancy***
- ***CSR / ESG Project Mgt***
- ***Carbon Reporting***
- ***Portfolio Modelling***
- ***Market Analysis***
- ***Forest Management***
- ***Project Feasibility***

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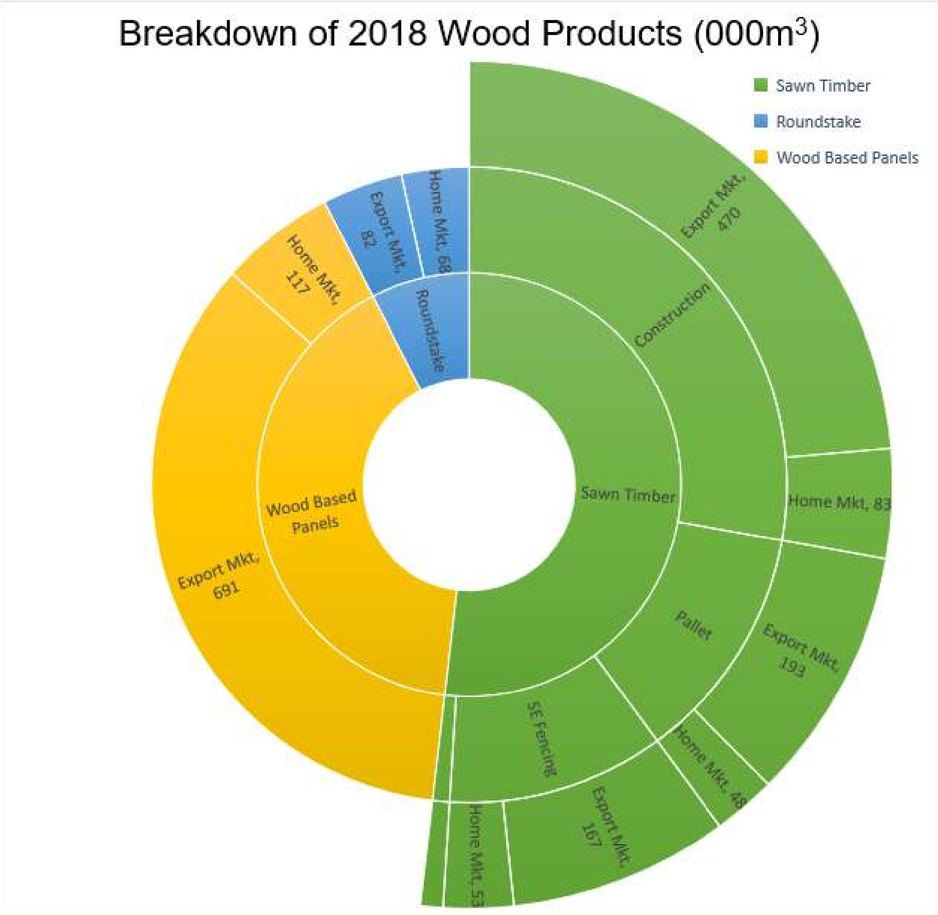
Irish Timber – Product Mix & Distribution



Data Source: COFORD Connects – Woodlfow and forest based biomass energy on the island of Ireland (2018)