

30 September 2022

Ministry for Primary Industries

By email: ForestryWoodProcessingITP@mpi.govt.nz

Submission on the draft forestry and wood processing industry transformation plan

Introduction

1. Energy Resources Aotearoa represents energy intensive businesses, from explorers and producers to distributors, sellers, and users, of energy resources like oil, LPG, natural gas, refined liquid fuels, biomass, and hydrogen.
2. This document constitutes our submission on the Ministry for Primary Industries (**the Ministry**)'s draft *Forestry and Wood Processing Industry Transformation Plan (ITP)*.

Scene-setting comments

We represent a breadth of stakeholders in the energy resources sector with a keen interest in forestry and the bioeconomy

3. Energy Resources Aotearoa has a keen interest in the draft ITP because we represent key players throughout the energy value chain. This includes:
 - a. electricity generators (Genesis) who are exploring the potential to fuel peaking generation at least in part by biomass;
 - b. liquid fuel importers and retailers (Mobil) who will soon be subject to a sustainable biofuels obligation;
 - c. large process heat users (Oji Fibre Solutions, Methanex) who currently, or in future could, use biomass as a feedstock and/or fuel source;
 - d. a range of energy and fuel sector service providers with interests in emerging fuels (including biofuels); and



- e. energy intensive businesses for which production forestry investments offer a cost-effective opportunity to offset residual emissions.
- 4. This places us in a unique position because we represent a breadth of existing and potential use cases for biomass resources. We expect some of our members will make their own separate submissions about the sector and their priorities for the ITP.
- 5. Our comments in this submission are therefore pitched at a New Zealand (rather than sector or business) level. Rather than focusing on specific measures floated in the draft ITP, we focus on principles to help inform their development and refinement.

We support the intent of the ITP and believe stable, durable, market-based policy settings are the best means to achieve it

- 6. We support the overall intent of the ITP – to maximise the value of New Zealand’s forestry and wood processing sector and to see it underpin the low-emissions economy. We support increased domestic high-value wood processing and manufacturing where New Zealand has a competitive advantage.
- 7. Government intervention will likely be required to realise the ambitions of the ITP. Our submission provides some guiding principles to inform the design and mix of interventions that support the right balance between costs and benefits.
- 8. Our general view is that government policy should be focused on identifying well-evidenced market failures and addressing them with solutions that are preferable to the status quo. Where government interventions – such as information, subsidies, or regulations – are pursued, these should lead to sustainably competitive markets in the long term.
- 9. The challenge facing New Zealand, as articulated in the ITP, is how to reconcile a growing range of potentially competing priorities for this high-value domestic resource (both domestic and global). Our starting point is that a well-functioning market and price signal is the most efficient mechanism to reconcile these competing demands over time. However, we recognise there may be market issues or failures undermining this mechanism, and where this can be established, we have offered our perspective on how solutions ought to be designed. We also recognise the forestry sector is exposed to a global market, and that the ITP needs to consider this reality.

Submission

- 10. The ITP signals a wide range of actions organised under its priority areas and key objectives. The sections below provide general commentary which looks at the different types of levers the actions envisage, and an indication of how we

approach thinking about these from a national policy perspective. We appreciate most of these actions will require further development and, in some cases, may be subject to further consultation on detailed proposals. We welcome ongoing opportunities to contribute to this process.

Facilitating well-functioning domestic markets for bioresources

Well-functioning markets are the best allocative mechanism we have for scarce resources

11. The ITP envisages a dramatic increase in both demand and supply of wood resources. Existing uses are likely to grow – the ITP targets a 25% increase in domestic construction demand, for example – alongside emerging uses such as biofuels for process heat and transport (particularly heavy freight, aviation and maritime) and bio-chemical manufacturing. A key question for New Zealand is how these competing demands will be prioritised, assuming woody biomass is a growing but still constrained national resource.
12. We are sceptical that this prioritisation should – or even can – be achieved primarily through central government planning or strategies. Supply and demand for wood resources will depend on technology economics and on pricing signals. This picture will change dynamically over time and will become more complex as the range of competing potential uses grows. Price is generally the best means to distil this complexity into clear, simple signals for investors.

Government should focus on facilitating and enabling these domestic and export markets

13. As noted above, there may be a role for government in facilitating and removing barriers to coordination or collaboration among market participants. A well-functioning market – both domestic and export – relies on participants (buyers and sellers) having sufficient information on which to make decisions about the future.
14. We support the ITP's proposals to improve transparency in biomass markets through up-to-date supply and pricing information, and through conducting regional mapping of biomass supply and demand. These may enable participants to identify strategic opportunities such as clustering and help to provide some confidence that supply exists to meet regional demand (and vice versa).

Subsidies and government co-investment

Where subsidies or co-investment are pursued they should be justified on a rigorous cost-benefit basis, and address genuine market barriers or issues

15. The ITP signals a range of actions which might involve government subsidies or co-investment – including:
 - a. government investment in growing wood processing capacity;

- b. supporting feasibility studies and business cases for regional manufacturing clusters;
 - c. supporting commercialisation of bioeconomy technologies and uptake of low carbon products;
 - d. funding options to support increased use of mass timber in construction; and
 - e. potential funding arrangements for investment in 'industry good'.
16. We generally do not support sector or technology-selective subsidies, on the basis that the market is the best means to achieve allocative efficiency between competing demand for scarce resources and to maximise community welfare.
17. We recognise, though, that in some situations, market failures may result in inefficient outcomes, and that subsidies are one among a range of potential government measures to address this. This might include addressing coordination issues to realise clustering or agglomeration benefits. These measures need to reach a high bar to be justified, given the significant potential opportunity cost of this public spending and the potential for market distortion.
18. Where a clear market failure is identified, subsidy proposals should:
- a. demonstrate that they will address the market failure, and do so in a way preferable to the status quo;
 - b. demonstrate that the benefits of the subsidy outweigh the costs (including opportunity costs), ensuring that government support is commensurate with the expected balance of private and public benefits; and
 - c. have a clearly identified 'offramp' – that is, condition(s) under which government support will taper off or cease entirely.
19. For example, the ITP notes that we have typically not processed our low-grade logs because this has historically been cost-prohibitive (particularly against an alternative of direct export, given global log prices). Emerging technologies offer an opportunity to process these lower-grade logs cost-effectively, but in some cases these technologies may suffer from a first-mover problem or the 'investment chasm' between proof-of-concept and commercialisation. We therefore welcome the recent announcement of a feasibility study at Kinleith to explore highest-value uses of wood residue at the site.
20. Where subsidies are provided to overcome this kind of problem, they should over the medium-long run result in a genuinely competitive and commercial market.

We see a comparatively strong case for government playing a facilitating role around access to capital

21. We are supportive of efforts to address genuine barriers around access to private capital through facilitation and provision of advice or 'matchmaking'. The ITP signals, for example, working with Māori to enable access to finance/capital to develop their own forestry assets, and facilitating new investment in the bioeconomy and advanced processing.

Standards and regulations

We support reducing regulatory barriers to activity

22. We strongly support government efforts to reduce regulatory barriers to economic activity. The ITP signals a number of these, including reducing non-tariff barriers to key markets, and streamlining consenting processes for development of new manufacturing and processing facilities.

We support a liberalised foreign direct investment regime

23. We have consistently argued that a liberalised foreign direct investment regime is in the long-term interests of New Zealand as it ensures we can continue to attract capital investment in a globally competitive environment. It is ultimately private finance that will fuel the growth in size and value of the forestry and wood processing sector that is envisaged by the ITP.
24. Further to this point, beyond the foreign direct investment regime – which directly impacts on foreign investment – more generally investment confidence relies on stable, durable policy settings across the board. Maintaining this ensures New Zealand is an appealing investment prospect amidst global competition for capital.

Government procurement rules to stimulate investment in wood processing should be subject to cost-benefit analysis

25. The ITP also signals that government could nudge the market through government procurement rules that favour wood-based solutions. While this is a 'softer' approach than a direct subsidy, such proposals will still need to stand up on a cost-benefit basis to ensure any costs (such as a cost premium for procured solutions compared to a status quo counterfactual) are outweighed by the expected benefits.
26. Such measures should be focused on using government procurement as a lever to address genuine market failures. They should be considered against alternative levers that are more specifically targeted at those failures, which would leave procurement to focus on least-cost procurement of goods and services.

The NZ ETS is a core regulatory driver of growing forestry supply

27. The primary objective of the NZ ETS is to establish a quantity-capped market for emissions to enable price discovery and a least-cost transition toward our 2050 national net zero emissions target. But we also recognise that a necessary flow-on effect of the scheme has been the significant additional incentive it creates for afforestation, which in turn contributes to the growing resource value the ITP seeks to harness. We therefore see regulatory stability around the NZ ETS as a key supporting factor in the success of the ITP.
28. We acknowledge the ITP considers issues around the NZ ETS as out of scope. Here we simply reiterate our position that the NZ ETS should be the central tool for delivering a low-emissions transition, and that to do this its settings should be kept stable. This will underpin long-term investment confidence for forestry providers, and for energy-intensive businesses seeking cost-effective means to offset their residual emissions.
29. We offer this view particularly in response to recent calls to limit afforestation through reform to the NZ ETS (rather than addressing this through a more targeted tool, such as a National Policy Statement which provides guidance on where forestry is desirable and undesirable at the margins). We are concerned by reports the Chair of the Climate Change Commission has increasingly called for a focus on gross emissions reductions, suggesting other countries were becoming increasingly sceptical about the use of offsets at all.¹
30. These comments may serve to significantly undermine investment confidence in the forestry sector given its existing role in the NZ ETS. There is an ongoing tension between the Government's desire for continued growth in the forestry sector on one hand; with increasing calls for limits to forestry's role in the NZ ETS to bolster the emissions price and to drive gross emissions reductions on the other.

Attracting, retaining, and developing a skilled workforce for the forestry and bioeconomy sectors

31. The energy resources workforce shares several key characteristics with the forestry sector. It is also male-dominated – though more women are joining the sector – and is aging. It contains a range of skills, including engineering, project management, and plant operations, that are highly transferable to emerging energy sectors (such as offshore wind and hydrogen). The emerging bioeconomy likewise presents a potential source of future demand for these skillsets, so we see opportunities for ongoing collaboration to build the vocational talent pipeline our sectors need now and in the future.

¹ For example, see <https://www.rnz.co.nz/news/national/475075/climate-change-commission-chair-dr-rod-carr-calls-for-reform-of-emissions-trading-scheme>

32. Energy Resources Aotearoa's forthcoming *Industry Skills Action Plan* for the energy sector outlines our approach, focused on attraction, retention/development, and collaboration. We would welcome further discussion with the Ministry and the Advisory Group to identify potential synergies and areas of cooperation on skills and employment.

Conclusion

33. We appreciate the opportunity to provide input and welcome further engagement as the ITP takes shape. We support the goal of maximising value from our forestry and wood processing sector and suggest that careful consideration of policy settings will be required to support the allocation of the resource to the highest value use, and to support a balance between costs and benefits.
34. We are particularly keen to engage with the Ministry and Advisory Group on the skills elements of the ITP, given the work we are leading in this space and the shared challenge we have in attracting, developing, and retaining the skilled workforce we need through the low-emissions transition.