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Acadian Timber Corp. 2013 Fourth Quarter and Year End Results Conference Call - Q&A Transcript

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Time: 10:00 AM PT

Speakers: Reid Carter
President and Chief Executive Officer

Brian Banfill
Chief Operating Officer

Erika Reilly
Chief Financial Officer

OPERATOR:

The first question is from Paul Quinn of RBC Capital Markets. Please go ahead.

PAUL QUINN:

Thanks very much. Just a couple of questions. One on, if you could -- weather has been particularly bad in Q1 here. Do you have an estimate as to how you've been affected, and what do you think in terms of, if you could quantify that impact on your operations?

REID CARTER:

We have had reasonable operating -- we had actually I'd say quite good operating environments into the last month, so in December of the fourth quarter. And then January, we actually had quite a bit of warmer and wetter weather that had some very, I'd say, modest disruption in our ability to operate and haul for maybe one or two weeks in January. We've returned to very cold and good operating conditions and I think the question is, we expect that we are going to have, I would say, a normal operating season. We do well with snow and cold weather, in terms of our own operations.

The question then becomes, does it impact home building; does it impact our customers, particularly our solid wood products customers' market? We believe most of our customers are still very bullish about the late winter-spring construction season, and are definitely trying to run full speed and build inventories and get their product to market.

So far, Paul, I would say we haven't really experienced any kind of disruption that would impact our typical first quarter, which as you know is plus or minus 40% to 50% of our annual operations, that occur in that first quarter. So it's an important quarter for us and so far, we're on track.

PAUL QUINN:

That's great to hear. And then just if you could give us what you're seeing, we're seeing markets improve overall. Do you have a volume guidance for any of the operations in New Brunswick and Maine, as to much more -- do you see an uptick in 2014 versus 2013? Could you give us any help on the modeling side?

REID CARTER:

Sure. I think as we have mentioned before, we operate in our New Brunswick operations under a fiber supply agreement that really is an even flow agreement. So we have not been significantly reducing or expected to significantly increase our harvest in New Brunswick, in relation to market opportunities. So I think you should expect harvest levels in New Brunswick to be very, very similar to last year. In terms of our Maine operations, the mix will change a little bit, but again, very much an even flow scenario. So you shouldn't expect big increases in relation to improved market opportunities.

PAUL QUINN:

Okay, great. That's all I had. Thanks.

REID CARTER:

Thank you.

OPERATOR:

The next question is from Andrew Kuske of Credit Suisse. Please go ahead.

ANDREW KUSKE:

Reid, could you just give us some context on what you're seeing or what you anticipate will happen with some of the wood flow dynamics in New England? And I ask that question in part because we saw the Verso deal for NewPage, and there's just some other activities going on in that neck of the woods. Do you anticipate any major changes just from the wood flow in that market?

REID CARTER:

It's a big question, Andrew. We think that it's -- going through the different products and customers, relatively quickly, the spruce fir sawlog, aimed at dimension lumber producers market, we think will be very strong. The concern always is having a healthy pulp paper industry, particularly a softwood pulp and paper industry, with the closing of the groundwood mills and the recent announcement by Great Northern for their residuals, and for their softwood pulpwood. As I mentioned, it's not a significant portion of our overall harvest volume and less of our operating cash flows, but it is an important part of the dynamic, and softwood pulpwood is being left in the woods on Crown Land in New Brunswick,

because of that lack of market opportunity. And biomass markets really don't offer similar economics to pulp and paper customers.

So I worry a lot about the softwood pulp side of the business. The hardwood side of the business, it actually depends on which products. Some of our customers, they don't all take every type of hardwood pulp, but despite all of the new capacity being built in Latin America, in particular, we believe that that market is -- in our particular region, is going to stay relatively robust for the foreseeable future.

The OSB, the aspen and poplar producers, have, very, very strong demand, and the hardwood specialty markets are just that, just specialty markets. We expect them to stay relatively stable.

I think the real concern in the region is if another major softwood pulp mill were to go down, just what the impact is on the margin opportunity for those softwood residuals. And then again; our saw mill, end-customer's ability to pay for sawlogs.

ANDREW KUSKE:

Okay, that's very helpful. On the biomass front, what have you seen with just customer behaviors in the last few months? Just in particular, as the power prices in the NEPOOL market have been so high. Has there been any change in behavior in trying to take down more product and trying to crank out more power?

REID CARTER:

I'm not fully informed on exactly what strategy each of our customers is using, but I think most of them are running full, but there hasn't been new capacity added in our local market. So we haven't seen a big change there.

We did see, when gas prices bottomed and the NEPOOL, the power prices were lower, we definitely saw intermittent operation and reduced local demand for biomass at that time, but we would say that is largely covered, and as I mentioned, we got new export demand, the New Brunswick operations, that are making that market tighter. The future of that market is entirely dependent on subsidies, whether in the U.K., Europe, New England, or elsewhere. I think that will be the bigger driver, as long as the biomass conversion and pellet industry continues, particularly in the U.K., which we think our



marketplace will stay reasonably tight, because that will be the new sources of demand; but it's still a small portion of our overall business.

ANDREW KUSKE:

And then just finally, you mentioned being hopeful on getting something done this year on the acquisitions front, and looking at North America and South America, and opportunities. Do you have any sort of color or granularity you can provide on the sort of size, with this just being in conjunction with some of the Brookfield funds, softwood, hardwood, eucalyptus plantations, just any color, that would be interesting from my --

REID CARTER:

We've offered, you know, Brookfield, to Acadian, and as we have mentioned, this is every opportunity is absolutely at the discretion of the independent members of Acadian's Board, is opportunity to participate in our private equity timber investments through Brookfield participation, in the two recently-raised funds, a Brazil-focused fund, and we will probably call it the Timber Fund Five. And those, in terms of geographies, those funds are focused heavily in the U.S. and Brazil, Australia, New Zealand, Canada, Uruguay, Chile, but the big emphasis on the U.S. Brazil, and maybe to us still dominant, but to a lesser degree Australia.

We have a very active pipeline and in some cases quite advanced pipeline, and some of these deals are at quite large scale, and others are smaller. But most of our transactions, unless they're tucking into an existing operating platform, we are typically looking at a total transaction values of more than \$100 million, and often up to, in the past, we've done \$2 billion transactions, but I think more \$100 million to \$500 million type size and Acadian would have some opportunity to participate in those.

Again, we are not showing anything to the Acadian's Board at this time. And then whether Acadian decided it was an appropriate transaction will be up to the independent -- a committee of the independent members of our Boards. So we're hopeful that we will make further progress on these transactions, and that we will show something, and that the Board will decide that they are a good fit, but not in the next month or so. But very hopeful that we will have some significant opportunities to present during 2014.

ANDREW KUSKE:

And I guess just following that, is Brazil becoming a lot more interesting, just given the fact there has been such a significant devaluation with the Brazilian Real?

REID CARTER:

There are a number of factors across Latin America. There is a tremendous amount of capital chasing a very, very thin marketplace in the U.S. right now, and we are very, very, disciplined in our underwriting. We clearly know what Acadian's investors expect. We've seen the return expectations of Acadian, that Acadian will be able to meet, in the last, well, since inception, and then Brookfield as a major shareholder, and as a major investor in the funds, all of these things keep us quite disciplined in this underwriting approach, and we're seeing the U.S. to be possibly frothy, but certainly full-valued and just as importantly, very thin opportunities.

Whereas in Latin America, capital markets are not closed, but they are certainly much tighter, both lending markets and equity markets. We've got some very aggressive growth plans on the part of many of the pulp and paper producers, but also some of the steel and pig iron producers, and I think the right thing to do when we're making investments is go where the opportunities are. So we are still very active in the U.S., but we will be looking hard, and working hard in Latin America as well.

ANDREW KUSKE:

That's very helpful. Thank you so much.

REID CARTER:

You're welcome.

OPERATOR:

Your next question is from Mark Kennedy of CIBC. Please go ahead.

MARK KENNEDY:

Just a question here on your – Acadian's harvest levels last year, overall. It looks like you're harvesting above your long-run sustainable yield, in both Maine and New Brunswick. And is that a case where you're just sort of clearing out lower-value fiber, and do you expect this to continue? I think

you said in Maine, that this -- or in New Brunswick, that this continues until 2021, so is this something we should look for, for the next six or seven years?

REID CARTER:

There's a couple of components to that. Always along with the yield is a very -- as I've described, a long-run measure, and then you have age class distributions that create a near and medium term harvest opportunity. So some of that is simply is reflected in the age craft distribution.

Since inception and we've talked, right back to our prospectus, we've talked about the strategy, where we expect that our overall harvest volumes will come down over time, but that our high margin harvest opportunities will increase, both in absolute, and more importantly, on a relative basis. So we have been converting some of our hardwood areas to softwood. And for a long time particularly back in the 1980s and 1990s, a big piece of that conversion was going on, and we'll be the beneficiaries of a greater softwood harvest going forward, despite having a lower overall harvest level. And our analysis suggests that this will have a net-net -- no net change on cash flow opportunities, on the cash generation. But really, it is a function of each class and species conversion that's been driving this.

It has not -- we're not concerned that we are creating any kind of hole that we will have to work, harvest opportunity shortfall that we will have to work our way through in the future. I'm very comfortable, what we're doing it sustainable. That is part of our SO-5 certification, to test that, and we have had no concerns on the part of our auditors.

MARK KENNEDY:

That makes sense. Thanks.

OPERATOR:

There are no more questions at this time. We will turn the conversation back conference back over to Mr. Carter for closing comments.



REID CARTER:

Once again, thank you very much for your interest in Acadian. We are always available. Certainly look forward to your questions. And we look forward to a good first quarter, reporting out to you in early May. So, thanks much for your time.

OPERATOR:

Ladies and gentlemen, this concludes the conference call. You may disconnect your lines. Thank you for participating, and have a pleasant day.