

TRANSCRIPT

STANDING COMMITTEE ON THE ECONOMY AND INFRASTRUCTURE

Inquiry into VicForests operations

Melbourne — 30 May 2017

Members

Mr Bernie Finn — Chair

Mr Khalil Eideh — Deputy Chair

Mr Jeff Bourman

Mr Nazih Elasmr

Ms Colleen Hartland

Mr Shaun Leane

Mr Craig Ondarchie

Mr Luke O'Sullivan

Participating members

Mr Greg Barber

Ms Samantha Dunn

Mr Cesar Melhem

Mr Gordon Rich-Phillips

Witnesses

Mr Vince Hurley, Chief Executive Officer, Australian Sustainable Hardwoods; and

Mr James Lantry, Manager, Special Projects, Hermal Group.

The CHAIR — Mr Hurley and Mr Lantry, thank you very much for being with us today. This is an inquiry into VicForests's operations. The evidence, as I am sure you are aware, is being recorded. Welcome to the public hearings of the economy and infrastructure committee. All evidence taken at this hearing is protected by parliamentary privilege. Therefore you are protected against any action for what you say here today, but if you go outside and repeat the same things, those comments may not be protected by this privilege. Could I ask you to speak for about 5 to 10 minutes, and we will open it up for questions shortly thereafter. I think you have already stated your names for the records, so go ahead please.

Mr HURLEY — Thank you, Chair. Vince Hurley, Australian Sustainable Hardwoods CEO. A very quick overview: Australian Sustainable Hardwoods is Australia's largest sawmiller hardwood timber processor, but also the key to our business is manufacturing. It was with interest that I listened to Mr McEvoy about how he deals with market issues the way we do. We have 3000 architects that are in our family, if you like, and we are manufacturers of finished products into the market and are constantly evolving and changing to suit the market. That is our business. It involves a large investment because you have logs, you have air-drying stock and you have finished stock to deal with, but more importantly you also then have feed stock for your manufacturing operation. We employ 230 people directly, many more indirectly, and our main market is manufacturers in Melbourne, although we do send to manufacturers in all states and overseas as well as part of that, particularly in our key specialist areas of large triple-glazed window components and in staircase components — our two primary components that we export.

With VicForests we have a contract for 155 000 cubic metres per year, and in four out of the five years of operating at ASH they have not achieved our buyer request, so we request a certain volume and they have not achieved that volume. The volume we have to request is plus or minus 155 000 cubic metres. So they have agreed to it and it is signed off in a contract, but they have not actually done that. That is counting this year, by the way, because there is just no way they will actually achieve the buyer operation plan for this year, which obviously leads to issues with our business, because we sell what we produce and our cash flow and our whole business is based on selling what we produce. Our unit cost of production is also dependent on that, so if we process less than what we are aiming to process, our unit costs of production go up significantly. We operate in two shifts across our entire Heyfield business. It is not like you can knock off an eighth of a shift. You are basically paying for an eighth of a shift but missing out on an eighth of the volume that you could have got, so it does cause us a lot of issues.

We are a little bit unique also in that we have an operational agreement with VicForests where we actually provide them with information on a daily basis. It is a two-way street, and we actually do work quite well together operationally on the ground. The main issue we have is dealing at a higher level with respect to supply issues and getting them recognised and getting them rectified, and that is the basis of our evidence that we are writing. In dealing with that, VicForests tends to look at things and perhaps ignore things in the hope they go away rather than actually admitting, 'Yes, we've got a problem we need to deal with, and this is the way we're going to deal with it', and we find that is a common problem across that level of VicForests, where it can be quite difficult for a company to have a problem resolved. James, did you want to go?

Mr LANTRY — We will make some remarks, if the committee wishes, in respect to some of the forestry floor activities, giving mindfulness to your terms of reference. I guess from our side there is the business-dealing side in the way in which business dealings occur with VicForests as an entity, and then there are of course the forestry-side activities as well that we see.

Mr HURLEY — We are in the unique situation where we actually have what we call a bush boss, or a resource manager, who is extremely experienced in what he does. He gets around the forest in the company of VicForests, but he is also well connected with virtually all contractors and cartage operators.

Mr LANTRY — It might be useful to add at this point that there is some question around this issue of — and there has been a very public discourse between us and the government around it — supply, where the government, through VicForests, has been able to provide us with 200 000 cubic metres over three years, whereas our current contracted take is up to 155 000 cubic metres per year. The question is: why can we not operate the business simply at the lower volume level? Vince will probably be able to add a bit more than I can on that.

Mr HURLEY — I note that Mr McEvoy's evidence before was that he operates a 12 000 cubic metre mill. Our issue at Heyfield is that we are not just a sawmiller; we are a timber processor but more importantly we are

a manufacturer. We have now five — up until last year four — factories each working two shifts and employing the bulk of our 230 employees manufacturing finished products for the market. What the afternoon shift gives us is basically double our production for the cost of the labour, so it is a very good situation to be in where you have covered all of your overheads and you have covered particularly your marketing. That family of 3000 architects is critical to us in getting feedback and receiving feedback, and I welcome you to have a look at our website. We are on every social media as well, and that is updated daily. So it is critical to us to cover those sorts of things.

Trying to operate the sawmill on a one-shift basis becomes very, very difficult without the unit cost of production in your favour. We buy logs, we process those logs into slabs, we dry those slabs, we process those slabs into feedstock for our manufacturing plant and then the manufacturing plants are producing finished products for the market. Decreasing your throughput by half and therefore taking off basically half your shift then lowers you into the realms of, instead of earning quite reasonable money upwards of 15 per cent on your funds employed, being down around the 2 or 3 per cent. That puts you very, very close to the mark as far as trying to operate that business successfully and having continuing investment, particularly in equipment. We have certainly in the last five years updated quite a substantial amount of equipment, and you have to do that to keep pace with the market, keep in front of the game and keep efficiencies coming through, particularly in manufacturing. At 80 000 cubic metres you would find that very, very difficult to do. It becomes a very difficult proposition at that level.

Getting back to the forest floor and utilisation, our bush boss sees a lot of things and is a very good operator on the ground. One of the things that he does constantly complain of — and we have a one-on-one operational meeting every month with VicForests — is log grading. When the log grading card was developed, it was back in 1986, 1987, 1988, and I was actually involved in that as a young Forests Commission person. It really did work well for a lot of years, because it basically graded the logs and put them to the best use, so the highest priced logs would go to the best use and so on. What has happened is contractors have gone from being a 15 000-cubic metre or a 20 000-cubic metre total product contractor to now being very large contractors — 50 000 or 55 000 cubic metres. It means that they are extremely fast and mechanical in the way they do things. They cannot have a guy on the landing with a tape and a chainsaw individually grading every log. Trucking configurations have also changed, so 90 per cent of the loads that come into Heyfield are delivered on B-double configurations now. So you have a whole range of things impacting on how logs are prepared.

The issue that you have got is that VicForests is losing grade because logs are now basically cut to truck length. A lot of the lower grade log buyers — the E-grade log buyers — that being Big Traffic, who only wants 5.9-metre long logs, and Dormit, who wants logs in pallet multiples, tend to get their logs cut first. If you have a log that is cut, and it creeps back into the B and C grades and it makes that length, that is exactly where it is cut. So that B and C travels off to the E-grade buyer.

We recognised that issue and proposed to VicForests, ‘Look, let’s not do that anymore. We’ll take that bit of E on the end of the B. We’ll change it around, and we’ll take that bit’. Unfortunately that was not considered by VicForests to be acceptable, and I think it is probably on the basis that they already have large contracts teed up with their main E-grade suppliers, and they have to fill them. They have contracts, and they have to fill them, so they will continue to supply logs that do contain higher grades into sawmills that are paying for lower grade timber. I think one of the purposes of having the inquiry might be to recognise that and say, ‘Perhaps we can do it better’. It is worth money to Victoria. It is certainly worth wood to us in that we would have an uplift in available volume if that was to occur.

The other issue is that if contractors are cutting to length, you tend to get lengths that perhaps are wasted on the forest floor rather than being utilised as well, because if it is not quite a truck length to go between the bolsters of a skel, then they cut it and leave it. So that is another issue.

I have got to mention, though, that on the ground our dealing one on one with the people from VicForests is very, very good; we do have a very good operational relationship. I have got to praise VicForests for that side of it. The salespeople that deal with us one on one are very good. We like dealing with them, and they try and take our concerns into account.

The CHAIR — Just a couple of questions from me. Do you find VicForests difficult to deal with?

Mr HURLEY — Operationally they are great to deal with. In negotiating contracts, they can be very difficult to deal with. In recognising problems and rectifying problems, they can be very difficult to deal with.

The CHAIR — How do you actually plan when VicForests does not come up with the quantities that you are expecting?

Mr HURLEY — That is very difficult. Fortunately in having a person on the ground who can perhaps estimate, in some ways better than VicForests might, what will be delivered, we try and adjust our production so it is fairly even. For example, if we are scheduled to receive 145 000 cubic metres of logs in a year and by Christmas we have 25 per cent of them, then obviously we are going to think about how we are going to get the rest in, and we discuss it with VicForests, and then we try and plan. This actually happened where they said they would get the full volume in but they did not and we had to adjust our production. We actually in some products, particularly our number one staircase product, ended up short supplying once that short supply came through.

The CHAIR — And that would have cost your company significant money, I would imagine.

Mr HURLEY — It did, yes, and reputation, because we compete with imports. So you have got to have service, availability, value, quality, price. Service and availability is where we kill imports. The others are more difficult to deal with. So service and availability is critical to our business, and that is why having service and availability from our suppliers, our whole supply chain, is critical in that process.

Mr LEANE — The volume last year — you were saying that over the last three years the volume you received was about 200 000?

Mr HURLEY — No. What James was saying was that we are now out of contract as of 1 July, so unlike Mr McEvoy, who got his contract signed at 4 hours to midnight, ours did not get signed at 4 hours to midnight. So what James was saying was that from 1 July what VicForests have offered us is 200 000 cubic metres over three years as opposed to the current supply of 155 000 cubic metres per annum.

Mr LEANE — So last year did you receive the 155 000?

Mr HURLEY — Last year we received 158 000 cubic metres, and that was the only year that VicForests have actually supplied over and above.

Mr LEANE — So did that volume make the mill profitable last year? Did the mill make a profit last year?

Mr HURLEY — Yes, it did.

Mr LEANE — So there was a dispute with VicForests and ASH around bills not being paid to VicForests earlier this year. Is that correct?

Mr HURLEY — It is a whole mixture of things where the dispute was raised and therefore the amount that was owed to VicForests was quarantined until after the dispute was resolved. The dispute is now settled and a payment plan put in place, and that disputed amount has been settled.

Ms DUNN — Thank you for your submission today. Just to understand in terms of the wood that you get into your mill, annually last year you got 158 000 cubed?

Mr HURLEY — That is correct.

Ms DUNN — I am interested to understand just in terms of percentage how much of that would go to construction timber. When I say that I mean structural subfloor, so timber you cannot see. How much would go to veneer appearance-grade timbers? I do seem to recall that there is a small portion that also goes to Australian Paper — it is a finer waste product. So I am just trying to understand — you get it in, percentage-wise how does it go out?

Mr HURLEY — Fortunately, Ms Dunn, you have been to the mill and had the presentation — and so has Mr Bourman, I might add. They have actually seen us in action.

The CHAIR — I must have missed the invitation.

Mr BOURMAN — It is in the mail.

The CHAIR — Thank you very much. It will get here by Christmas then.

Mr HURLEY — Appearance grade is our number one product, and it constitutes about 65 per cent of our sales volume. Structural constitutes around about that other 35 per cent, but if you divide it up into iron ash and our other range, around about half of that 35 per cent is going to appearance structural. So our absolute number one aim is that the appearance structural market is on our hit list — to actually grow that and get out of hidden structural, if you like. Hidden structural can be the domain of plantation pine, LVL, all of those products. Let them have it. As far as we are concerned our target is to keep going along that visual appearance, and that might be things like big post and beam construction that you are seeing in a lot of buildings now — —

Ms DUNN — Like exposed beams?

Mr HURLEY — Not so much — very different. There are a number of new projects on our website that you can look at where there are great big 400 by 400 millimetre posts, 7.2 metres long, with big connecting beams and then glass between them, in a four-storey office building. That is a key market because it can be done by our product, particularly our iron ash product, and it looks great and it is a very high value end use. That is a target for us. So that is basically 65-35, and of that 35 about half is going into what we call appearance structural.

Ms DUNN — So that was your sales, but that is not necessarily representative of your volume, is it?

Mr HURLEY — In volume terms, around 29 per cent of our total volume of our intake goes to Australian Paper in the form of woodchips, which I think is the question you are asking.

Ms DUNN — No. I am still trying to get a sense of — so the balance, 71 per cent, you have got veneer appearance and then also construction structural subfloor hidden timber. What would be the split between those?

Mr HURLEY — What do you mean by ‘veneer’? If we put appearance grade or higher value in one case — —

Ms DUNN — Let me phrase it another way. You have 71 per cent left. You produce a whole lot of products. Some of them are used in construction you cannot see and some of them are used and you can see. That is the division I am after.

Mr HURLEY — It is a mathematical thing. Out-the-gate recovery of timber products is just under 40 per cent, remembering that around about 17 per cent is shrinkage, because we dry our timber, unlike Mr McEvoy. About 17 per cent is shrinkage, so our out-the-gate recovery is just under 40 per cent. Of that 40 per cent, 65 per cent is appearance grade and then you have 35 per cent left over. Half of that 35 per cent is appearance structural and the other half of that 35 per cent is structural structural. Then the balance is sawdust that we sell into the chicken meat market.

Ms DUNN — I just want to talk about reductions that were flagged in volumes in May 2013 by VicForests, and that was clear, I think, in their corporate plans, and I think there were even media releases around that. Back in 2013 it was flagged that there had to be volume decreases. I am just wondering, given that industry knowledge around those reductions, why a decision was taken to scale up staffing and production at the Heyfield mill knowing that into the future there would be an impact on resource.

Mr HURLEY — What VicForests also said then was the first thing is McCormack Demby voluntarily closed. That was a 65 000-cubic metre sawmill that closed. VicForests also transitioned to other sawmills — that is, out of Ashington species. So that accounted for the 28 per cent reduction in sustainable yield that Ms Dunn is referring to that was a result particularly of the 2009 fires but also other things. That left a critical mass of volume that enabled them to offer us a 155 000-cubic metre contract per annum until 2034. They offered that in February 2014 and, as we have already said, that contract took some time to negotiate and was not signed at 1 minute to midnight before the previous government went into caretaker mode.

Ms DUNN — That is an excellent segue to my next question, which is exactly about that contract that I think got a mention in a couple of newspaper articles. It talks about that 130 000 to 150 000 cubic metres to 2034 and

talks about it being signed by VicForests directors Rob de Fegely and Therese Brian. I am just wondering, can you provide the committee with a copy of that contract as evidence?

Mr HURLEY — Yes. I cannot see any reason why not. I can email that to — —

The CHAIR — Lilian, yes.

Mr HURLEY — Lilian.

Ms DUNN — Terrific.

Mr HURLEY — I will provide that, yes.

Ms DUNN — The secretariat will be in touch with any follow-ups as well. That would be very helpful. This is a difficult question, and you might want to take this on notice because I am actually reading it from a submission provided by VicForests which I do not think you have had the liberty to see yet. The reason I ask the question is because it is talking about changes to log grading at the Australian Sustainable Hardwoods mill. It is essentially saying that there have been very little changes to log grades in relation to inspections undertaken out there at Heyfield. Perhaps I can ask on notice that you maybe turn your attention to this submission when it is available and provide some feedback to the committee on, I guess, your comments around what is provided in here, because I do not want to read the report out but I think that —

The CHAIR — It is probably very good thing, Ms Dunn.

Ms DUNN — you should have an opportunity to respond to that particular matter.

Mr HURLEY — Can I ask when that would be available.

Ms DUNN — Do we have to vote to publish that?

Ms TOPIC — Yes. Within a few days.

Ms DUNN — Yes, so it will not be too long.

The CHAIR — Do you have any more questions, Ms Dunn?

Mr LANTRY — Is there anything specifically in that report you wanted to look at? Is it the grading?

Ms DUNN — Yes, it is the grading. There is a section called, ‘3.4 Sawlog customer monitoring and audit loads’. I do have a couple of questions. Should I wait?

The CHAIR — If you are kind enough to wait now, we will fling it over to Mr O’Sullivan and see what he has got. We will get back to you on that one.

Mr O’SULLIVAN — Thank you, Chair. I have got a couple of questions I would like to ask Mr Hurley in relation to his business. The government is going to buy your business. Is it for sale?

Mr HURLEY — That is probably a better question for the shareholders or the representatives of the shareholders in the next session, because that is their responsibility. It is not my responsibility to comment on that.

Mr O’SULLIVAN — In terms of the government going through a process of buying a business such as yours, of which you are the CEO, I would imagine that the government would have come to you to understand what your books are and so forth so they can get the information from you guys in terms of preparing a business case for sale. Have they been to you guys and sought your details in terms of figures and so forth in relation to a business case that they would prepare to buy your business?

Mr HURLEY — The information was actually already provided because as part of going through this process — and Mr Tilley was deeply involved in this — after the announcement in January this year of the decrease in volume, a working group was set up to interrogate what the economics are around the business and

what is going on. As part of that, a very, very detailed submission of all of our financials including audited financials, volume throughputs — the whole lot — was prepared by Pitcher Partners. And we paid for that.

The government had a firm called PPB interrogate that data and also then prepare a report. Based on that, there is a lot of very detailed information about the business that the government had already. The government then informed — only just very recently — the shareholders that they would like to talk to the management. That blessing was done, and it has only recently occurred that the management and the government have been able to talk on the basis of what the business might look like. However, that is currently on hold. You could ask Mr Tilley that later about what is happening in that space, because until you have a sale process, that process cannot continue anyway.

Mr LANTRY — If I could, Mr O’Sullivan, the information that was provided to the government during February and March was provided on the basis of our understanding that they were assessing us for this question of assistance for retooling, not for the purpose of sale.

Mr O’SULLIVAN — I will hold some of those questions, but I just want to go to a couple of other things more specific to Mr Hurley before we move on. It just goes to the question of volume of timber. As Ms Dunn has just indicated, the contract in 2014 that VicForests and ASH agreed on was in the vicinity of, what, 130 000 to 150 000?

Mr HURLEY — No, 155 000 cubic metres per annum was effectively the volume that ASH could take on an annual basis. That varied down to 135 000 cubic metres. It depended on what the request by ASH was prior to any particular year starting in April.

Mr O’SULLIVAN — And was that through until 2034?

Mr HURLEY — 2034.

Mr O’SULLIVAN — Okay. That was at the end of 2014 and agreed by VicForests and you. Now we are in a situation where that number has come down to 80 000 cubic metres, because the press release that was issued by the Premier in February had the words that VicForests said that was the amount of timber that was available to make the timber industry sustainable. What happened to the timber in those short few years where VicForests agreed to 135 000 to 155 000, but now it is only 80 000?

Mr HURLEY — That is a great question that perhaps we would like answered as well. So that is our key, in that up until the date that Mr Tilley met with Mr Trushell of VicForests and was informed of 80 000 cubic metres, our business was going ahead on the basis that the volume was there. VicForests would normally release a resource outlook, but they had not released one while the whole task force process was going on. So really we understood that the volume would be available until the point that Mr Trushell informed Mr Tilley that it was 80 000 cubic metres. So that is a big unknown to us. Since that time we have had a presentation by VicForests of, if you like, where the volume has gone. It is not entirely satisfactory to see exactly where it has gone, but my understanding — —

Mr O’SULLIVAN — Was it burnt in a fire?

Mr HURLEY — No, because the 2009 fires were already taken into account. The sustainable yield dropped by 28 per cent. One of the keys that they are pointing to is that they were planning on a certain net harvestable area being available, and that has been impacted by a number of things. The number one thing has been the Leadbeater’s management action plan, which is reserving more and more and more areas — the fact that at the moment, because it does not have a cap on how many reserves might be created, they have got to allow for that process to continue. And it will continue on at the current rate, so therefore they have got to say, ‘Well, if it continues on at the current rate, there will be so much more forest reserved for the Leadbeater’s management action plan and therefore there will be less available for the timber industry’. That is the number one.

Mr O’SULLIVAN — So you are saying that they are reserving forest areas now in case there might be possums in the future.

Mr HURLEY — Correct. They are building that into their modelling. So they are saying, ‘Well, currently we have so much reserve created because of Leadbeater’s possums being detected’.

Mr O'SULLIVAN — But didn't they say they will review the 200 coupes?

Mr HURLEY — Yes, there were supposed to be a review after 200 sightings, and that review has never taken place. So we are up to 617 — I think it was on the website last time I looked — sightings. There is a review. My understanding is that the minister for environment is supposed to be reviewing that based on a report given to her by ARI at the end of April and actually reviewing what should be happening with the Leadbeater's management action plan. But currently VicForests must plan on what they know, and what they know is that it appears those sightings will continue. Therefore, looking into the future, if those sightings continue, then they have to plan for that — that there will be more and more area that will be unavailable for the industry.

The other factor that is built into their modelling is that what they get off a particular coupe area has decreased. This is particularly in relation to what are called net harvestable areas. So if they planned that the net harvestable area in a coupe would be 18 hectares and the gross area of the coupe might be 21 hectares and the net harvestable area is 18, what is actually occurring is they are getting 15 of 14 cubic hectares being harvested rather than the net 18 that they originally proposed or thought they would get. That is built into the model too, further lowering the sustainable yield. They are the two main factors. In my questioning of VicForests, they have basically said 70 per cent Leadbeater's, 30 per cent other including the net harvestable area changes.

Ms DUNN — Can I just ask a follow-up? It is just on the Leadbeater's.

The CHAIR — I thought you would be onto that like a seagull on hot chips. Mr O'Sullivan, before we go back to the possums.

Mr O'SULLIVAN — I think I understand the volumes. So we have gone from 155 down to 80 as a result of possums that may be there in the future.

Mr HURLEY — Correct.

Mr O'SULLIVAN — I just want to go on to what the impacts to your business might be as a result of the disappearing quantities of timber. I understand that now there are about 260-odd jobs that you have got at ASH.

Mr HURLEY — So there are 230 direct and 20 contracted jobs on site in Heyfield.

Mr O'SULLIVAN — And is that now at 158 000 cubic metres?

Mr HURLEY — 155, yes. We are basically selling at the rate of around about 147 500 cubic metres of log equivalent.

Mr O'SULLIVAN — So what happens to your business if you have dropped down to 80?

Mr HURLEY — In the case of the current shareholders, it is basically something they cannot do because you cannot carry the overheads and the debt and everything of 155 000 at that level. That is why there has to basically be some sort of government purchase or assistance or help with transition to another business. So the current shareholders could not do that.

Mr O'SULLIVAN — What happens if, for instance, the government came back to you and said, 'We'll increase your volume, say, to 80 000 this year, 80 000 next year and 80 000 the year after'. What would that do in terms of employment at your business?

Mr LANTRY — One of the critical issues that we have is that what has been offered has been 80 000, 60 000 and 60 000. That is it. To undertake a change to the mill to be able to operate at a lower volume would involve a significant retooling exercise to be able to have those margins at a level where we could function. You cannot invest in a business when you have no certainty beyond that three-year period and the level of required investment — —

Mr O'SULLIVAN — Sorry. What is offered beyond the third year of 60?

Mr LANTRY — There is nothing offered beyond the third year. VicForests was very clear about their offer. It was 80, 60, 60 and then we will see what happens after that in terms of what they could actually offer the

business, so we had no certainty first of all in anything beyond three years and, secondly, you have then got a volume level that cannot function in the current business structure.

As Vince made clear, we are an import competitor where we are not the cheapest but do offer consistency of product and the range of supply. That fundamentally has changed when you have a significantly lower volume that is available to you and you lose the ability to be able to gain that margin benefit from second shifts and those types of things, which enable the business to be at a level where it is profitable. When you have a position where that is what has been offered, you actually have an unsustainable, unviable business.

Mr O'SULLIVAN — One last question from me: 230 jobs plus the overflow of the 20 other indirect jobs — —

Mr HURLEY — They would be direct jobs as well, but with contractors — electricians and so on.

Mr O'SULLIVAN — How many other jobs around the whole of Victoria, for instance, would your business directly impact if you are no longer — —

Mr HURLEY — Directly just in our Gippsland area where we very much concentrate on using local suppliers — —

Mr O'SULLIVAN — And I guess your timber also comes into Melbourne for a whole range of furniture and so forth.

Mr HURLEY — We actually did surveys as part of this exercise. We went to our three major distributors. We sell to large manufacturers directly, but for a lot of the small manufacturers we go through distributors. Fifty-five per cent of our product is sold in Victoria, and Victoria really is the hub of timber manufacturing in Australia. What we found when we did the survey was we said, 'Go to your customers that you supply ash to and ask (a) how many employees they have and (b) whether that business was highly dependent, moderately dependent or lowly dependent on being supplied ash'. Just with three distributors, which represents around 55 per cent of sales or 56 per cent of our sales in Victoria, they came back to say 6700 jobs are directly impacted by our supply, of which a third is highly dependent.

If you extrapolate that to the other customers in Victoria that we did not survey, because we — —

Mr O'SULLIVAN — Another 45 per cent.

Mr HURLEY — Well, it is around 10 000 jobs in Victoria that are directly dependent on the ash business for finished products. We are not sending sawn timber to them; what we are doing is, for example, with staircase manufacturers we send stair treads that are cut to length — 930 millimetres, 1 metre, 1.1, 1.2, 1.4, 1.6 — sanded, finished, ready to assemble. It is the same with stringers; it is the same with window profiles in our large end section window business — laminated, profiled, set length. Those businesses depend on that manufactured component because, if they were just to get the sawn timber and try and laminate up and do it themselves, they just could not do it. They would be inefficient, and they would have recovery losses through the cutting of timber.

We have two finger jointers at Heyfield, a very highly mechanised business, as Mr Bourman and Ms Dunn have seen, and we basically use the offcuts. So if we are making stair treads that are 1 metre long and the pieces of timber are 1.8 metres long, we will use that 0.8 and we will finger joint it up into another product that might be actually going into a window component that we laminate together. By having an integrated manufacturing business, we can do it profitably. But, more importantly, our customers, particularly in Melbourne, can receive components that are ready to use, and they can compete with products that are coming in from overseas. In particular there is a lot of finished flat pack staircase coming into Australia now. They can outcompete them at the moment because they have got ready-made stair treads and things to be able to use. So that is in manufacturing.

The other thing worth pointing out is that we are the only domestic supplier into Bunnings of finished benchtops for Kaboodle and panels into Bunnings. Every single other benchtop and every single other panel in Bunnings is imported, and that is Australia-wide. It is those sorts of things — that is, finished, shrink wrapped, cut, with all of the packaging and all the instructions, in the case of Kaboodle, on the benchtop ready to be used.

Mr BOURMAN — Regarding one comment you made about the change to B-doubles, I am just a little bit curious. Has the overall length of the log shortened to fit on a B-double? How did that actually become part of this conversation?

Mr HURLEY — It has come about because in the forest operation you have a very, very fast process on the landing. It is going through quite quickly, so in order to make sure that the log will be suitable to go onto a truck, it has to be a certain length, basically above 4 metres long. In order to do that, they basically make sure it is above 4 metres long. The other thing with a B-double is you have got a front bay. The logs have to be between 4 and 6 metres. So you have got to fill that bay and there are often three bays, so you have got three bays of 4 to 6 metres or you have got a front bay, which sometimes is around the back now, but basically a front bay of 4 to 6 metres and then a back bay of roughly 8 to 12 metres as well.

The truck configuration is only part of the story. It is more that the guys do not have time to get down, look at every log in detail in order to determine where the B changes, where it becomes C, where the C becomes D and where the D becomes E. They have basically got to cut it to length. The easiest way to do that is the lowest common denominator has the higher grade attached to it.

Mr BOURMAN — Getting on to grading, I did take the time to read the utilisation procedures of VicForests, although I would hardly call myself an expert, and I see that you have supplied us with a picture here about the C-grade logs being used for pulp, for instance. Going into the utilisation procedures manual — this is going towards how VicForests deal with it — it says that VicForests takes responsibility basically if there is a problem. On the ground, how have you found this to be? Just being careful, I guess, in the context of our other discussions, has this been a process that has generally been fairly easy?

Mr HURLEY — Can you repeat the question please, Mr Bourman?

Mr BOURMAN — Given that there is a fairly set procedure with how it is meant to work, is it working that way with VicForests?

Mr HURLEY — No, it is not working all the time that way. There has been a drift into lowest common denominator or average log grading, and that is the problem we see and that is why we proposed a different solution to maximise that. That is probably a question to actually ask VicForests: are their log utilisation and log grading procedures being followed? They can produce certain audits and things to say, 'Oh, yes. They look good'. That is very interesting.

In our submission, VicForests were to contract a company called Interpine from New Zealand to review their utilisation procedures and review how they were operating on the ground. We were informed in one of our operational meetings verbally that their board had requested that on the basis that the board perhaps thought they were not getting as much out as they could. I note that despite us being told for probably four or five months that that was going to occur, Interpine was never engaged and therefore did not interrogate the utilisation procedures of VicForests.

Mr BOURMAN — I am just using the C-grade picture here. Would you have any rough idea of how many tonnes, if there are any tonnes, going to pulp that could be used to go to the mill?

Mr HURLEY — No, I do not. That is very hard. Probably the better question may be: how many tonnes of high-grade sawlog is going into E-grade sawlog? On the face of it, if you look at 2008, the total cut of D-plus ash was above 300 000 cubic metres and the cut of E-grade sawlogs was 155 000 cubic metres. Next year the cut of D-plus is dropping to 130 000 cubic metres and the supply of E-grade is 150 000 cubic metres, and that has progressively happened. I do not think the forest has changed that much that suddenly there are more lower grade logs being thrown up, so that probably answers it.

Mr BOURMAN — During the presentation I got out at the mill there was a proposed change to the grading procedures, which would have a lot more usable timber out of the same tree. If the magic wand could be waved and that was available today, would the change in grading and the reduction in the amount of timber supplied still make the mill viable?

Mr HURLEY — To be viable on two shifts you really cannot drop below 130 000 cubic metres. That is probably the key. Given that VicForests are saying that the volume available of C-plus logs to ash is

80 000 cubic metres I am not sure whether changing the log grading would actually get another 50 000 cubic metres to actually put that in. There is a proposal we put to them to actually investigate. We did this back in February, and in fact Bruce McTavish from VicForests and our bush boss, Ross Britton, did go out to the forest together and start that process, but then VicForests stopped that process.

Mr BOURMAN — So to cut a long story short, we do not know.

Mr LANTRY — There is a picture of what you are referring to on page 47 of that draft, which was the change to the tree and how you actually utilise the tree cut. The estimate is around a 20 per cent gain in actual take from each tree.

Mr BOURMAN — Have the government explained how they think 80 000 tonnes a year is going to be viable when you do not think it is?

Mr HURLEY — It has only been in the last week and half that the government and the management have been able to talk directly about how 80 000 cubic metres may be a viable business. We have stopped that conversation now until Hermal and the government can reach a consensus on the sale price for the mill, so it is a work in progress. I think there can be changes to make it a viable proposition to be able to operate at 80 000, but there are some key levers that, I think, would need to be adjusted in order to make a viable business at 80 000 cubic metres, including landed log price and a couple of things like that.

Mr BOURMAN — With the proposed retooling for the smaller logs — there was a figure mentioned, but again we will assume that someone comes up with the cash and it is still 80 000, so still not working on any more timber tonnage — with that retooling, and it goes in, is it still going to be able to keep the same number of jobs in the mill, or are we going to lose some if that is the case?

Mr HURLEY — No. Since we have been talking to the government we have done some modelling on employment at 80 000 cubic metres, so the 230 direct employees now will drop to 120 direct employees. That would be 110 positions that would not be available in the mill at 80 000 cubic metres.

Mr BOURMAN — And is that even with the retooling to be able to use the smaller logs?

Mr HURLEY — Yes.

Mr LANTRY — There are probably two processes of change. The first is that smaller logs need a fundamental change to the green mill, which would likely involve the construction of a new green mill to be able to handle the smaller log size. The benefit of actually doing that upgrade is that as plantation timber comes online you are actually able to then process that timber, because you need a different saw process for those timbers. To make further and other viability changes to the mill at lower volumes you have to change the dry mill processes and do a significant amount of automation in a number of the dry mill processes. So you have got two areas of change: one is about the smaller log end and being able to utilise the smaller logs and being able to create and generate a viable business through that process, and then the second component is what you actually do in the dry mill. That is probably the biggest issue. The bottom line is you have to cut the number of staff. You have to automate that business.

Mr BOURMAN — You either have the logs or you have the jobs.

Mr HURLEY — Well, in managing a business you have got to ensure that you minimise risk. One of the key increases that you have is increase in labour cost, and that happens every year. It is one of those key things that you have got to manage.

The CHAIR — Ms Dunn tells me she has one clarifying question.

Ms DUNN — I do, thank you, Chair. It was in relation to some evidence you provided to Mr O'Sullivan, in relation to how much reservation had been set aside for Leadbeater's possum. I just wanted some clarity. Because you talked about it being a 70-30 split in terms of the issues around supply, I am just wondering: were you referring to the temporary exclusion of around 15 000 hectares of forest, of which 73 per cent is already in national parks and conservation reserves, which comprises, I think, 0.5 per cent of the total ash forest, or were you talking about the buffers that have been put in place for Leadbeater's possum, which equate to 2983 hectares, which is 1.2 per cent of the total area of ash forest available?

Mr HURLEY — What VicForests is saying is — and what I was saying in answering Mr O’Sullivan’s question — it is the buffers and the reserves created by Leadbeater’s and other Leadbeater’s issues that flow on from that in perpetuity. I would encourage you to get the VicForests resource outlook; you may already have that.

Ms DUNN — You would be talking about this flawed calculation, I am guessing.

Mr HURLEY — That is the one.

Ms DUNN — Yes, the one that actually contains mathematical errors.

Mr HURLEY — Right.

The CHAIR — We will get to that a bit later.

Ms DUNN — Do not worry, you do not have to answer VicForests’ maths.

Mr HURLEY — You do not have to worry about that.

Ms DUNN — That answers my question, Mr Hurley. It is actually based in a fantasy, but that is not your — —

The CHAIR — Thank you very much.

Ms DUNN — I have other questions, but I am happy to lodge them on notice.

The CHAIR — Thank you very much for coming in, gentlemen. Thank you for your evidence. You will receive a transcript in the next little while. If you have a look at that, make sure that everything is as it should be, as I am sure it will be, and get it to us, that would be marvellous. We thank you very much for coming in today. It is much appreciated.

Witnesses withdrew.