



Timberland Investor Report

U.S. Timberland Returns Remain Subdued but Stable in a Turbulent 2020

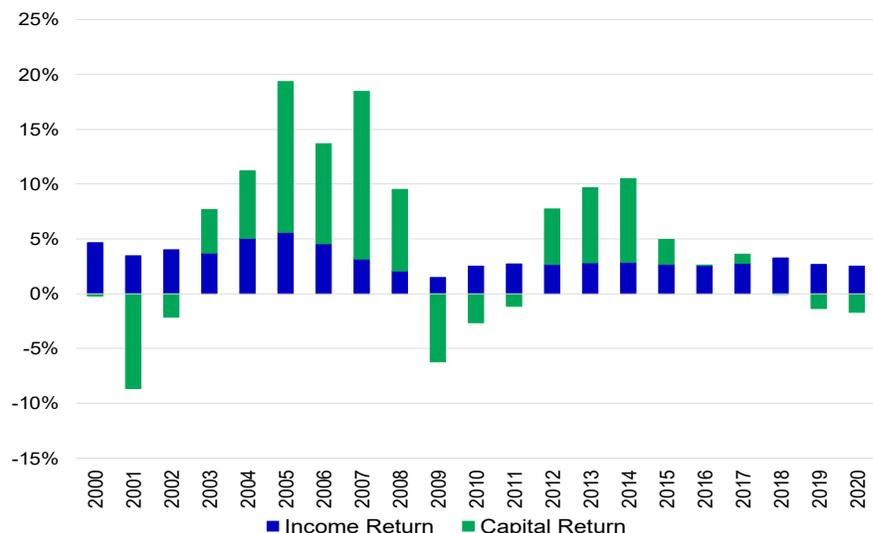
NCREIF reported the U.S. Timberland Index posted a market value-weighted 0.81 percent in 2020, a decrease of 49 bps from 2019. Across the major U.S. regions, annual returns ranged from -4.75 percent in the Northwest to +2.91 percent in the Lake States.

As in prior years, we devote our fourth quarter issue of the Timberland Investor Report to a review of NCREIF's year-end report of the return performance of U.S. private timberland properties. The NCREIF (National Council of Real Estate Investment Fiduciaries) Timberland Property Index¹ (TPI), tracks the returns realized by institutional investments in U.S. timberland properties. NCREIF also tracks the performance of timberland commingled funds and separate accounts, through the Timberland Fund & Separate Account Index (TFSAI).²

In 2020, the TPI incorporated data from 460 timberland properties with a combined area of 13.0 million acres across the U.S., and a combined market value of \$22.6 billion. As a subset of the total TPI, the TFSAI tracked fund level data from 10 managers in the U.S. managing 92 funds with a combined market value of \$18.1 billion.

U.S. Timberland Performance Retreated to 0.81 Percent in 2020

Chart 1. NCREIF U.S. Timberland Property Index, Annual Income and Appreciation, as of year-end December 31



Source: NCREIF, December 2020

¹Hancock Timber Resource Group is a participating member in the NCREIF Timberland Property Index. The Index requires participating managers to report all eligible properties to the Index. Usage of this data is not an offer to buy or sell properties.

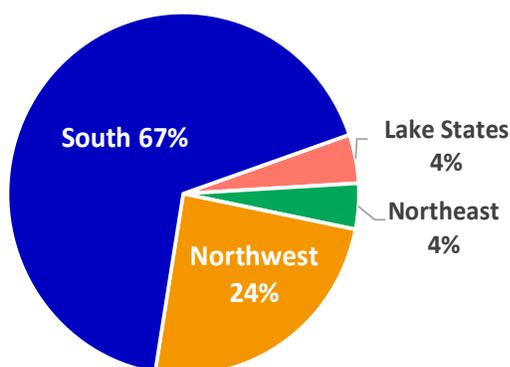
²Hancock Timber Resource Group is a participating member in the NCREIF Timberland Fund & Separate Account Index. The Index requires participating managers to report all eligible properties to the Index. Usage of this data is not an offer to buy or sell properties.

In calendar year 2020, the TPI's total return of 0.81 percent was the lowest annual return since 2010, and was 3.8 percent below the average annual return level of 4.6 percent in the last decade. The TFSAI posted a gross total return of 0.73 percent, which was well below the 10-year average of 4.1 percent for the TFSAI.³

NCREIF separates total returns into two components: net operating income (EBITDDA⁴) and capital appreciation. In 2020, U.S. net operating income slipped to 2.5 percent, which was down from 2.7 percent in 2019, and slightly below the average annual income over the past ten years (2.8 percent). Net operating income for U.S. timberlands in 2020 was negatively impacted by the global economic downturn that started in early 2020, when economic activities were limited and trading was brought to a halt due to public health concerns during Q2 and Q3 of 2020. Yet, negative impacts were moderated by strong U.S. housing markets in the second half of 2020, leading to strong demand for wood products while regional and local supplies were limited. In the second half of 2020, lumber and wood panel prices surged to historical highs, pulling timber prices up in the last quarter of 2020, resulting in income returns edging up towards the end of 2020. The capital appreciation component of the TPI is based on annual third-party appraisals of timberland market values for all properties included in the NCREIF Timberland Index. In 2020, the combined market value of U.S. timberland properties in the TPI decreased by -2.3 percent, after seeing a -1.7 percent decline in 2019. The declines in market values are driven by negative appreciation returns in three of the four NCREIF regions in 2020, i.e. South, Northwest and Northeast.

Timberland Properties in the Northwest and South Comprise nearly 92 percent of the U.S. NCREIF Timberland Property Index

Chart 2. Regional Share of the Timberland Property Index by Value (as of December 2020)



Source: NCREIF January 2021

NCREIF timberland performance is reported for four regions within the U.S. (Lake States, Northeast, South and Northwest). The U.S. TPI is heavily weighted toward the South, which represents 67 percent of the index by market value.

³The TFSAI reports the total gross return before accounting for investment advisory fees, based on changes in published fair market value net assets.

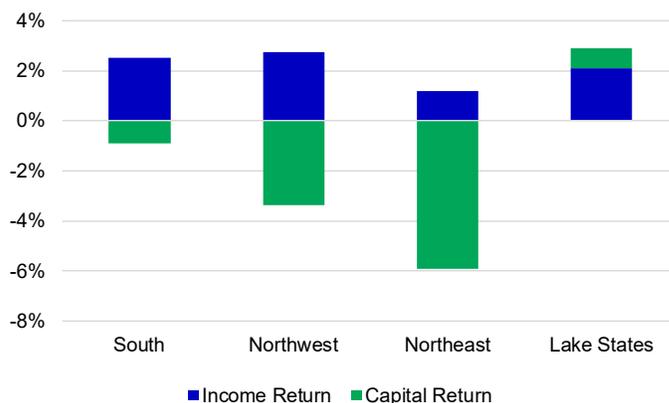
⁴EBITDDA: Earnings Before Interest, Taxes and Depreciation, Depletion and Amortization.

The southern timberland properties in the TPI are predominantly pine plantations. Northwest timberland properties represent 26 percent of the U.S. Index by value and the remaining 8 percent of the U.S. Index value is split between the high-value hardwoods and mixed softwood/hardwood timberland in the Northeast (4 percent) and the Lake States (4 percent).

Accounting for nearly two thirds of the market value of the overall TPI, private timberland in the U.S. South faced headwinds in both income returns and capital appreciation. Net income returns for 2020 in the South remained positive at 2.5 percent, but was slightly down from 2019 although still holding level with the region's 10-year average income return. The region's ample inventory of timber worked to hold prices down despite record-setting prices for finished forest products. Capital appreciation during 2020 for southern timberland within the TPI was -0.9 percent, as appraisers adjusted forward-looking price expectations downward in light of the muted timber price response to strong demand from lumber and panel mills in 2020. Yet, this moderate decline compared favorably with the sharper contractions in capital appreciation registered in the Northwest and Northeast.

Positive Operating Income in 2020 Offset by Negative Capital Returns in the Most Regions

Chart 3. Annual Timberland EBITDDA and Appreciation Returns by Region in 2020 (data as of December 31)



Source: NCREIF January 2021

Private timberland investments in the U.S. Northwest, which account for over a quarter of the market value of the overall TPI, experienced a -0.7 percent total return in 2020, which was a more moderate decline than the previous year when total return slipped 2.4 percent. In calendar year 2020, a 2.8 percent annual income return, the highest among regions, was offset by -3.4 percent capital appreciation, producing a negative total return.

Income returns in the Northwest benefited from strong housing markets for most of last year and record setting lumber and panel prices. However, capital appreciation in the Northwest suffered a sharp reversal (-3.4 percent) in part, reflective of the lagging impact of the correction in the region's timber prices that occurred between 2018 and the first half of 2020.

Downward Pressure on Regional Capital Appreciation Weighs on 2020 U.S. Timberland Return

Table 1: Regional U.S. Timberland Calendar Year Performance, 2020

	South	Northwest	Northeast	Lake States	U.S.
EBITDDA	2.51%	2.76%	1.21%	2.12%	2.50%
bps change from 2019	-33	24	-76	-2	-18.4
Capital	-0.89%	-3.38%	-5.90%	0.78%	-1.66%
bps change from 2019	-101	142	-201	-332	-132.5
Total	1.61%	-0.69%	-4.75%	2.91%	0.81%
bps change from 2019	-136	169	-278	-340	-191.2

Sources: NCREIF Q4 2020, HNRG

Total timberland returns in the Lake States at 2.9 percent out-performed all other regions in 2020, moderating from the 6.3 percent total return achieved in 2019. The 2020 Lake States operating income of 2.1 percent, was above average for the region (average income over the past ten years is 1.5 percent). The Lake States saw increasing property counts and acreage in 2020. The region was the only U.S. timberland region to experience positive gains based on property appraisals, which boosted the capital appreciation component of the Lake States TPI by 0.8 percent.

U.S. Northeast timberland experienced significant challenges in 2020. The region's total return, at -4.8 percent, was the lowest across the U.S. timberland regions. Operating income in the U.S. Northeast was 1.2 percent in 2020, the second lowest in the past decade (96 bps lower than the 10-year average). Timberland values in the region also saw the second largest decline in a decade, registering a -5.9 percent decline in 2020. The suppressed income returns and negative capital appreciation reflected in part, the soft demand outlook for timber products in the region in the wake of the imposition of trade restrictions by China in 2019 on hardwood logs and lumber.

U.S. timberland returns in 2020 reflected sector-wide market conditions, including: the impacts of trade restrictions imposed in 2019; market disruptions in both domestic and exports markets due to the COVID-19 pandemic; a swift recovery in U.S. housing markets in the second half of 2020; and an on-going recovery in consumption of forest products and demand for timber products. Looking forward, as the nation moves to post-COVID normalcy, timber prices and timberland returns are expected to continue the rebound that began in late 2020, as both exports and domestic demand gains momentum.

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