Hancock Timber Resource Group®
A Manulife Asset Management Company

OVERVIEW

Institutional investment in timberland accounts for more than $40 billion according to Hancock Timber Resource Group year-end 2007 estimates. Historically, investments in timberland have provided total real returns (net of inflation) of 6-10 percent, and nominal returns of 9-15 percent.

History of timberland investing

In the US beginning in the mid-1970s, two forces accelerated institutional ownership of timberland: passage of the Employee Retirement Income Security Act (ERISA) in 1974, and increasing sales of timberland by large forest products companies. The ERISA laws encouraged institutional investors to diversify away from traditional fixed-income securities, and led them first to greater investment in stocks, then to investment in other assets such as commercial real estate. Ownership of timberland real estate provided yet another opportunity for diversification. During this same period, forest products companies began to evaluate the strategic role of their timberland holdings. Some saw the value in their forests, particularly in the underlying land, as potential capital. These companies could sell their timberland, with the proceeds being invested in wood-processing facilities. This, however, raised the question of who would buy the land. Pension funds and other institutions with vast amounts of capital, and a legal mandate to diversify their investments, became logical buyers of this timberland.

Natural investment characteristics of timberland

A unique characteristic of timberland is that it functions as both a factory and a warehouse. In other words, timber can be grown and then "stored on the stump." This gives investors the flexibility of harvesting trees when timber prices are up, and delaying harvests when prices are down. Timber is also a renewable resource that increases in value as trees mature. Consequently, larger diameter trees are disproportionately more valuable than smaller ones.

Timberland investment risk

The primary risks of timberland investing include market uncertainty (fluctuation of timber and timberland prices), relative illiquidity (compared to stocks and other financial assets) and environmental risk (natural hazards or legislation related to threatened or endangered species). An experienced forest management firm can mitigate these risks, and geographic diversification of timberland further offsets risk associated with a specific region.