KPMG’s Timberland Investor Sentiment Survey

A prosperous outlook with the global recovery

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Executive summary

Investment in timberlands has been an attractive alternative investment strategy over the past several years, with investors continuing to act as net buyers of timberland assets despite ongoing volatility in global economies. With U.S. housing starts approaching all time highs and forecasts expecting U.S. housing starts to exceed record levels, demand for timber continues to be robust. Annual housing starts are expected to reach 1.5 million in 2019, which is higher than the pre-recession level of 1.3 million in 2007. Other growth will be driven by demand from China, who is set to phase out commercial logging of natural forests by 2017, which will lead to an increase in demand in exports to China as it is expected that 40 percent of China’s timber demand will have to be filled by timber imports by 2020. We still observe a rising number of institutional investors, hedge funds, and private equity funds increasing allocations to timber investments throughout the United States and the rest of the world. Our experience working with investors and managers confirms the attraction to stable cash flows, current yields and inflation hedging characteristics. An increasing number of market investors has led to significant investment in the industry and a rise in sophistication on the part of investors. KPMG’s Timberland Investor Sentiment Survey provides insight into investor profiles, attitudes and certain underwriting criteria, as well as forward looking sentiment on timberlands as a distinct investment class.

The KPMG survey
KPMG LLP’s (KPMG) Forest Products practice conducted a survey of a broad array of entities that invest in timberland assets throughout North America. Overall observations include:

— Discount rates have shifted downward, on average, compared to 2015 KPMG survey results.
— While respondents continue to be net buyers of timberland, significant investment outside North America continues to follow a downward trend.
— The majority of survey participants expect log pricing to remain the same or increase slightly in the next 5 years, as prices have started to trend to pre-recession levels.
— The majority of respondents noted they utilize no real growth rate over the term of their investment for harvesting costs as inflation stagnates for the United States.

Survey objectives
The survey’s objectives are to accumulate and evaluate feedback from a variety of market participants regarding key investment underwriting assumptions and forward-looking investment sentiment relative to timberland investments over the next 12 months.

Methodology
KPMG conducted a Web-based survey during July 2016. The survey was distributed to timberland executives. Survey results are distributed in this annual publication on a blind basis to ensure confidentiality for survey participants.
1. Please describe your firm’s structure.

- 39%: Timberland/ Appraisal/ Consulting Organization
- 22%: Integrated Forest Products Company
- 22%: Timberland Investment Fund Manager
- 9%: Real Estate Investment Trust
- 9%: Timberland Lender

*May not equal 100% due to rounding*

2. Please describe your role.

- 33%: Chief Executive Officer
- 25%: Asset Management
- 29%: Chief Financial Officer/Controller
- 13%: Timberland Valuations Professional
- 9%: Chief Investment Officer

*May not equal 100% due to rounding*
Where in North America are your Timberland Investments located? (Select all that apply)

- 54% Coastal Northwest and Alaska
- 46% Southeastern United States
- 38% Northeastern United States
- 33% Interior West
- 33% Midwest
- 25% California
- 21% Canada
- 17% Southwestern United States
- 13% Not Applicable

Multiple Responses Allowed
4. What real discount rate do you use when evaluating new acquisitions of timberland assets?

Discount rates on average continue to shift downward.

5. Over the next 2 - 3 years do you expect the real discount rate to increase, decrease or stay the same?

The vast majority of this year’s respondents expect real discount rates to remain relatively flat over the next few years. However, some respondents are expecting discount rates to further decrease compared to results from the 2015 KPMG Survey.
(Among those who expect the real discount rate to change over the next 2-3 years) By how much do you expect it to change:

The majority of respondents continue to utilize an investment term between 0 to 20 years, followed by an increase in the number of respondents utilizing an investment term of more than 50 years. The respondents are generally utilizing the same investment term compared to the 2015 KPMG Survey results for the other investment terms. However, the shift to using 0 to 20 years or greater than 50 years likely represents the effort to model another full economic cycle as the timber industry reaches pre-recession levels.

May not equal 100% due to rounding.
What growth rate for timber harvest costs (on a real basis) do you assume per annum over the term of your investments?

The majority of respondents noted they utilize no real growth rate over the term of their investment, which is close to the current rate of inflation of 1.0 percent.

What growth rate for operation and management costs (on a real basis) do you assume per annum over the term of your investments?

May not equal 100% due to rounding.
What growth rate do you assume for log prices (on a real basis) per annum over the term of your investments?

The majority of respondents indicated they assume a real growth rate greater than 0 percent to 2 percent over the investment term.

Over the next 5 years do you expect log prices (on a real basis) to increase, decrease or stay the same?

The increase in the log price growth rate can be attributed to the increase in housing starts. US housing starts in 2016 are expected to continue increasing over the next five years to 2021 indicating a strong current demand in the future for log prices.
Among those who expect the log prices (on a real basis) to change over the next 5 years. By how much do you expect log prices to:

- Increase
  - Greater than 0% to less than 2%
  - 2% to less than 4%
  - 4% to less than 6%
  - Greater than 6%

- Decrease
  - 6% to less than 8%
  - 8% to less than 10%
  - 10% or more

Do you expect market export volume to increase or decrease in the next 3-5 years?*

- Increase 57%
- Decrease 35%
- Stay the same 9%

* Does not equal 100% due to rounding
12. Do you expect an increase or decrease in the number of domestic sawmills in operating circles over the next 3-5 years?*

- Increase: 25%
- Decrease: 4%
- Stay the same: 71%

13. How long do you assume it takes to market and sell your timberland investments?

- Less than 1 year: 79%
- 1 year: 17%
- 2 years: 4%
- 3 years: 0%
- 4 years: 0%
- 5 years or more: 0%

A growing number of respondents expect marketing to take less than one year compared to the 2015 KPMG Survey.
What is the most significant variable to your risk profile? For each, please rate on a 1 to 10 scale, where 1 is not significant, 5 is significant and 10 is very significant.

- Government involvement in the industry
- Changes in Forestry Practices
- Changes in Product Types (i.e. plywood vs. OSB)
- Changes in Sawmill Technology
- Changes in Land Use (i.e. HBU, conservation easement, alternative land use)
- Increasing spread of disease and invasive pests (i.e. Pine Beetle)
- Global Warming (fire, floods, drought)
- Other

May not equal 100% due to rounding.

Government involvement continues to be the most significant factor to respondents’ risk profiles while changes in forestry practices replace changes in land use as the second most significant factor when compared to the 2015 KPMG Survey. Increasing spread of disease and invasive pests, and global warming are the least significant factors.
Investor sentiment

**What is your current portfolio species mix?**

![Current Portfolio Species Mix Graph](image)

The portfolio species mix is similar to the ideal mix with the exception that respondents prefer Pine and Hemlock and more Douglas Fir and Cedar.

**What is your Ideal portfolio species mix?**

![Ideal Portfolio Species Mix Graph](image)

Data is calculated by taking the average of percentages.
In 2017 do you anticipate being a net buyer or net seller of timberlands?

- Net Buyer: 71%
- Net Seller: 29%

The majority of respondents, 71 percent, continue to be net buyers of timberlands, indicating that acquisition targets will have multiple bidders.

Do you plan on making any significant timberland acquisitions in the next 12 months?

- Yes: 55%
- No: 45%

55 percent of respondents plan on making significant timberland acquisitions in the next twelve months. This represents an 18 percent decrease from the 2015 KPMG Survey.
What percentage of your annual harvest do you plan for export in the upcoming year?

- 0 to less than 25%: 64%
- 25% to less than 50%: 5%
- 50% to less than 75%: 27%
- 75% or more: 5%
- N/A: 5%

A majority of respondents surveyed plan to export little to none of their annual harvest over the next year indicative of strong domestic demand.

Do tax rates influence your investment decision making process? (buy, hold, sell strategy)

- Yes: 63%
- No: 38%

Respondents continue to indicate that taxes influence their decision making process.

May not equal 100% due to rounding.
**20a** On a scale of 1 to 10 (with 10 being the highest influence), how influential is the consideration of taxes in the investment decision process?

- 1–4: 13%
- 5–7: 53%
- 8–10: 33%

-May not equal 100% due to rounding

**20b** Does the U.S. proposed tax reform affect your investment decisions?

- Yes: 33%
- No: 67%
International interests

Do you have significant timberland interests outside North America?

- Yes: 17%
- No: 83%

May not equal 100% due to rounding

More respondents indicated they do not have significant investments outside North America, a continued trend since the 2012 KPMG Survey results.
KPMG’s Forest Products practice

KPMG’s experience serving clients in the forest products industry is extensive. The size and scope of our Forest Products practice makes KPMG one of the most effective service providers for the forest products industry in North America. KPMG has long had a commitment to and extensive involvement with the forest products industry (including timber, wood products, pulp, paper, and packaging).

Our dedication to the industry is evidenced by KPMG’s Global Center of Excellence for the Forest Products Industry. The Center’s role includes developing a worldwide market focus, recruiting experienced personnel, staying abreast of issues affecting the global forest products industry, developing products that add value to the industry, and providing thought leadership. KPMG provides professional services to over 65 percent of the world’s largest forest products organizations and audits 70 percent of the top 10 F1000 Forest Products companies.

Our Forest Products practice serves a wide spectrum of companies in the industry, including entities that are treated as C corporations, S corporations, and partnerships for federal and state tax purposes.

KPMG’s commitment to the forest products industry means that we have the experience and knowledge to help our clients understand and address the issues affecting their business. Our Forest Products practice professionals have extensive experience in the industry. They are committed to staying current on emerging technical and business topics, and KPMG continually invests in new technology, tools, and other resources to support them.

Our focus is on serving companies in your industry and your value chain so they can bring immediate value to your business. Importantly, we can provide perspectives on industry-leading practices to examine key issues and mitigating risks, thereby adding value to our engagements beyond generic accounting and tax matters.
For more information about KPMG’s Forest Products practice or KPMG’s Timberland Investment Sentiment Survey, please contact the following KPMG professionals:

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