

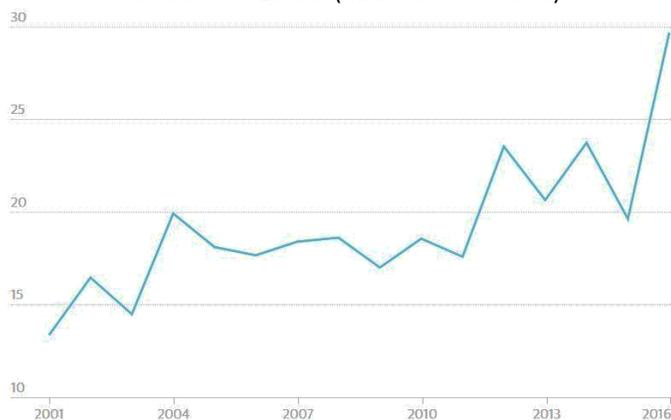
plant-a-tree fund - Forestry and Timber Info Sheet

Long-term Trends in Timberland and Wood Industry Investing

Welcome to this sixth edition of “plant-a-tree fund – Forestry and Timber Info Sheet”! More than presenting a global snapshot of the forestry and timber industry at the moment of publication, this short brief aims to present useful information on trends in timberland. These topics may cover diverse areas, such as geographies, species, markets, and price trends.

It’s difficult to resist the view that the wood industry may be approaching a watershed moment. On the one hand, insatiable global demand for wood products, particularly from China, shows no sign of diminishing. Between 2012 and 2016, Australia tripled its wood exports to 3.6 million cubic meters with 96% destined to China.¹ On the other, deforestation and degradation of natural forests has continued unabated, perhaps not coincidentally in areas buffeted by the booming timber trade: the state of Queensland, Australia saw a 33% rise in tree clearing in 2015-16.² Forest losses represent depletion of future lumber stocks and ultimately raise the marginal cost of a major source of supply.

Global Tree Losses (millions of hectares)



Source: Carrington, D. “The seven megatrends that could beat global warming: ‘There is reason for hope’”. *The Guardian*. 8 Nov 2017.

Against this backdrop, climate change has wrought havoc on North American lumber markets. BMO’s Forest Products Index jumped to a record high, largely the effect of a demand spike driven by Hurricanes Harvey and Irma and simultaneous wildfires across British Columbia that cut supply.³ Oriented strand board prices surged to a 13-year high and Canadian lumber stock prices have risen relentlessly through the year.

Political momentum around forest restoration has accelerated. Policymakers increasingly realize that reducing deforestation and planting new trees are among the most cost-effective ways to reduce carbon emissions and deliver a third of the decarbonization needed to meet Paris Climate Agreement targets.⁴ Efforts such as the Initiative 20x20, which aims to restore 20 million hectares of forest in Latin America by 2020, recently announced US\$2.1 billion in earmarked investment.⁵ Such policies will undergird a gradual transition from forest logging toward managed tree plantations.

Jeremy Grantham, GMO’s respected analyst of long-term trends and an opinion leader in timberland investing, recently qualified his market view.⁶ He conceded that high corporate profit margins and low interest rates may persist longer than previously believed. Dispelling market boosters, however, he maintains that valuations will ultimately revert by as much as two thirds toward their mean over the coming two decades as inflation and interest rates inevitably rise. In other words, commodity inflation is likely to kick in within a reasonable horizon for most investors. What effect might this have on timberland and the wood industry?

Structural constraints on standing timber stocks coupled with increasing land use competition from farming and urban development collectively have bolstered the profile of timberland whose return derives from land appreciation, biological growth and timber prices. Historically, timberland has provided an effective inflation hedge, a fact which may draw investors seeking refuge from rising inflation. Although markets have been quiescent with the S&P hovering at all-time highs, macro trends may eventually trump central banks’ ability to manage the interest-rate environment with unpredictable consequences for markets. Investors are well-advised to consider an allocation to timber to hedge risk while gaining exposure to an asset class with a steady tailwind behind its sails.

Canadian Lumber Companies Stock Prices



Source: Owram, K. “Nafta Impasse Draws a Yawn as Canadian Stocks Near Record High.” *Bloomberg*. 23 Oct 2017.

Sources: 1. Ekstrom, H. *Wood Resources International*. 7 Nov 2017. 2. Robertson, J. “‘Alarming’ rise in Queensland tree clearing as 400,000 hectares stripped.” *The Guardian*. 5 Oct 2017. 3. “The Goods: Commodity Recovery Back on Solid Ground.” BMO. Oct 2017. 4. Griscom B. et al. “Natural climate solutions.” *PNAS*. Vol. 114 no. 44. 5. “STATEMENT: Landmark \$2.1 Billion Earmarked to Restore Degraded Lands in Latin America, Offering Global Climate Solution.” World Resources Institute. 9 Nov 2017. 6. Coumarios, J. “Jeremy Grantham predicted two previous bubbles. And now?” *WSJ*. 5 Nov 2017.

Andrew Miller, Independent Forestry Consultant