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Southern Timberlands

Millions of acres are changing hands and hardwood pulpwood is fetching prices higher than pine pulpwood.

TIMBERLAND MARKETS

Millions of Southern timberland acres were on the market at the beginning of the year. Industry is continuing to raise capital or shed non-strategic assets by disposing of timberland. International Paper announced plans to sell 1.5 million acres in the region over the next five years. Louisiana-Pacific announced plans to sell about 600,000 acres in the South and Rocky Mountain regions. Weyerhaeuser announced plans to sell nearly 550,000 acres in the South. MeadWestvaco is selling 850,000 acres, about 200,000 of which are in the South.

While it has been "normal" for industry to sell timberland in recent years, there have been some differences in this year's offerings. While large numbers of acres are being sold by these companies, the timberland is being sold in smaller parcels, many of retail size. As a result, there are some new buyers in the market. Some of the industrial timberland is being purchased by institutional investment managers, but many parcels are being sold to wealthy individual investors or real estate speculators.

Institutional investors have also been active. The California retirement system, CalPERS, put over half a million Southern acres on the block early in the year. Some of these lands went to other institutional investors. When accounting for these and other transactions, it appears that there will be a net gain in institutional timberland acres in the South this year, in spite of the CalPERS sale.

PULPWOOD MARKETS

Pine pulpwood prices in the South declined steadily between the first quarter of 1998 and the third quarter of 2002 (Figure 1). As we noted in previous issues, causes for the price movement ranged from industry consolidation to weather conditions and insect infestations.

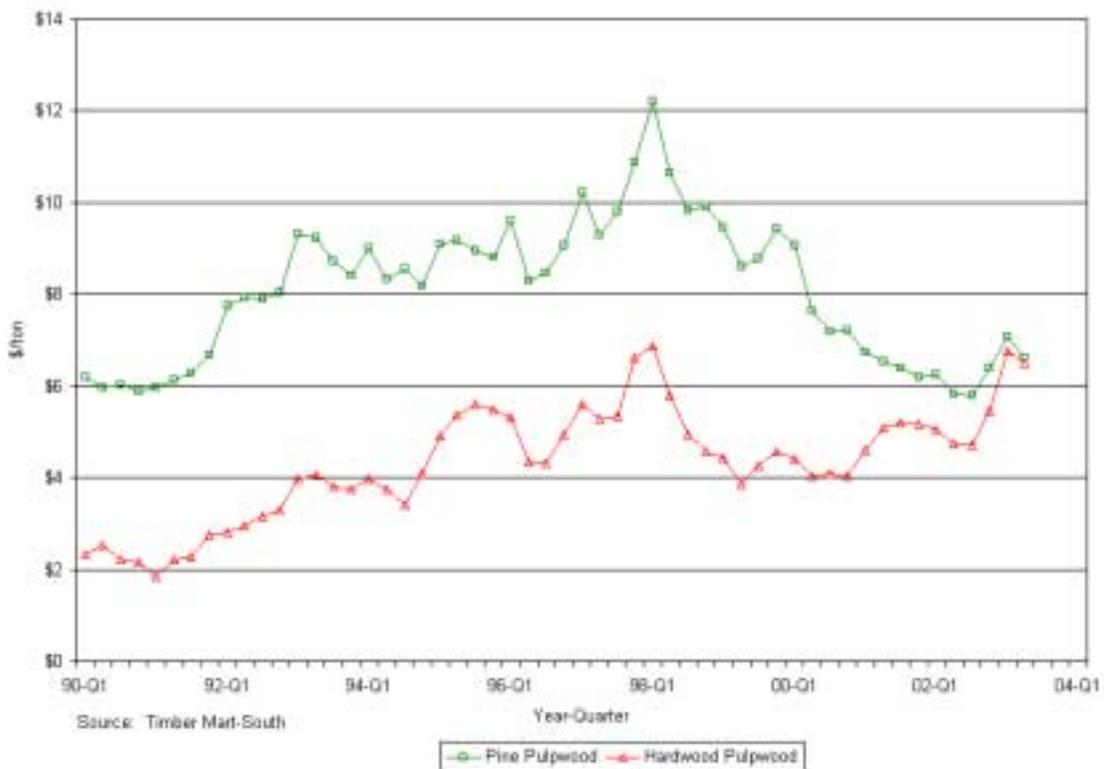


Figure 1. Recent Southern Pulpwood Stumpage Prices

Industry may be reaching the point where its consolidation efforts are slowing a bit. Over 3.2 million tons of paper capacity were permanently shut down nationwide in 2002, according to the American Forest and Paper Association. There have been a few more closures in 2003, but some temporarily closed mills have reopened. Market pulp prices have shown some strength during 2003. Strong demand for pulp translates into strong demand for pulpwood.

The South suffered through a multi-year drought into 2002. Dry conditions allowed loggers to operate year-round, and reach timber on ground that would normally be too wet to log at certain times of the year. However, record levels of precipitation over the past 12-15 months in some areas have put some wood under water and rendered some timberland inoperative.

The wet weather began driving pine pulpwood prices up during the fourth quarter of 2002. However, *nominal* prices are barely above what they were in 1990.

Rain can have an especially strong impact on the hardwood resource. Pines are planted on the upland soils, soils with better drainage and operable during normal precipitation conditions. The hardwoods, however, grow in natural stands on the side and bottoms of the valleys (bottom lands). The slopes are more subject to erosion during wet periods and the bottoms are subject to flooding. As a result, the heavy rains this year have reduced the hardwood harvest in many areas of the South.

Figure 1 shows that hardwood pulpwood stumpage prices have risen almost to the level of pine pulpwood prices. In fact, there are market baskets in the South where the hardwood price has exceeded the pine price during the year. Southwide, hardwood pulpwood prices are three times higher than they were in 1991 and 50% higher than they were in 1999.

LARGE TIMBER MARKETS

Figure 2 shows Southwide stumpage prices for larger logs.

Hardwood sawtimber prices have been steadily increasing over the past 13 years. They are now nearly 3 times higher than they were in early 1990. While rising hardwood prices might be good news for timberland owners, most large southern properties contain a high proportion of pine, and relatively small amounts of hardwoods.

An optimist might say that chip-n-saw prices have stopped their decline and are leveling off. A pessimist might say they are still declining.

Figure 2 clearly shows a decline in the difference between pine plylog and sawtimber prices. This is a result of the loss of plywood's share of the panel market to reconstituted panels, primarily oriented strandboard (OSB).

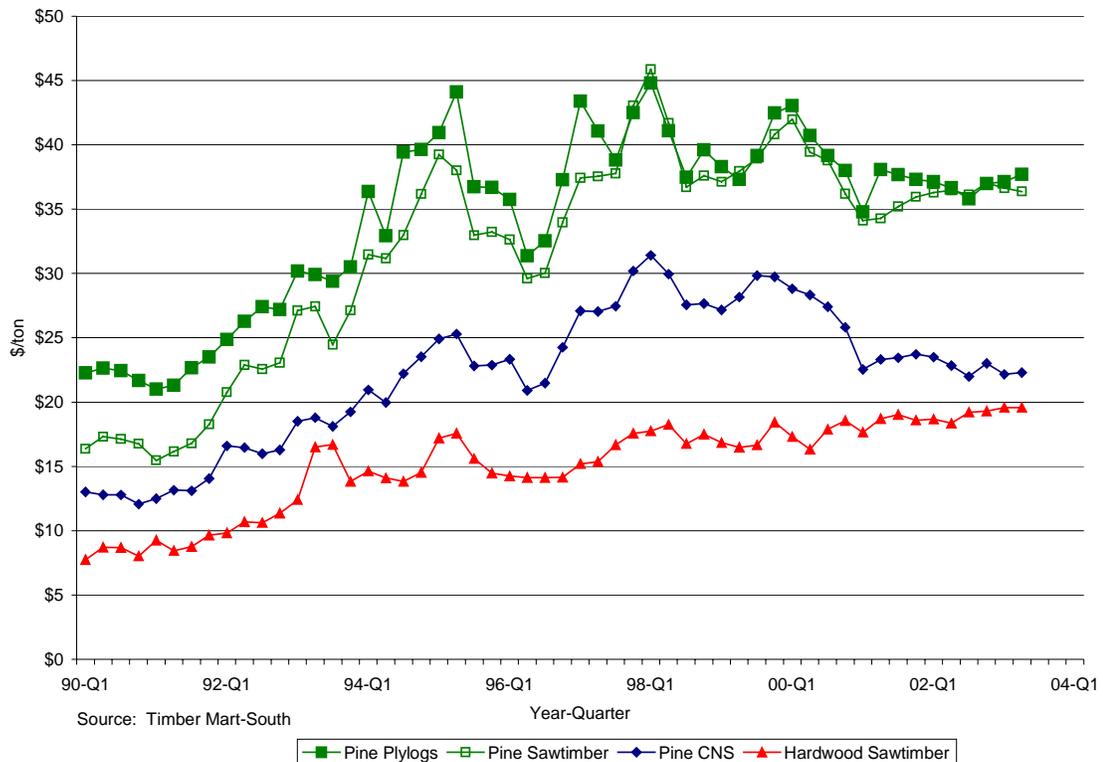


Figure 2. Recent Large Timber Stumpage Price

TIMBER AND TIMBERLAND VALUES

Figure 3 shows pine stumpage prices and Southern timberland values as indicated by the NCREIF Timberland Appreciation Index for the South.

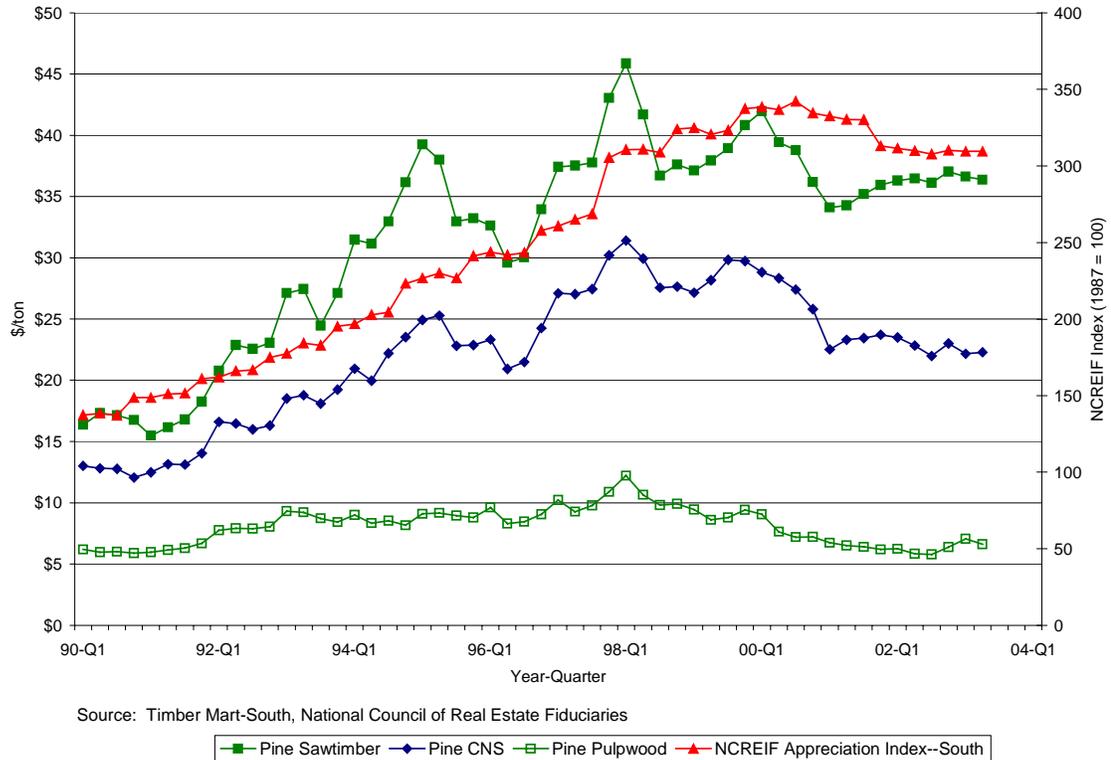


Figure 3. Timber and Timberland Values

The chart suggests that declining timber prices have contributed to a decline in timberland values since 2001. While timber prices undoubtedly contribute significantly to timberland value, we cannot tell from the chart what role the supply of and demand for timberland itself has played in the decline in timberland values. It is possible, for example, that the millions of acres of Southern timberland offered for sale in the last two or three years have exceeded the demand for timberland - or, at least, have exceeded the capital available to buy it.

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