UPM TILHILL AND SAVILLS FOREST MARKET REPORT
Introduction

At the start of the global financial crisis back in 2007, few would have been bold enough to predict the extraordinary performance of the UK forestry sector which, according to the IPD UK Forestry Index, is showing an annualised total return of 17.7% over the past five years and 16.3% over the past decade.

Looking back, we can see that the rapid rise in the capital values of woodlands was initially driven by investors seeking a secure asset in which to shelter cash. The potential tax reliefs, coupled with a surge in interest in renewable energy opportunities and long term optimism in timber prices, fuelled interest in the sector. Existing investors looking to increase their woodland holdings, new investors entering the market for the first time, and large forestry investment funds acting for pools of investors, all led to a surge in demand.

While 2013 began with concerns that the UK might slip back into recession, as the year progressed an improvement in the economy has led to early signs of growth. The forestry market remained extremely active throughout the year, with the highest level of total area sold since 2009. It has been strongly supported by a number of forestry investment funds and high net worth individuals, who have been active at the top end. Both sectors of the market have been aggressively bidding for good quality spruce forests, which offer reasonable scale and access to timber markets. We envisage that the value gap, between prime and slightly poorer quality woodlands, will continue to widen in the same way that there is polarisation between the best and the rest within the agricultural land market.

As the wider economy continues to recover, there is short term speculation that capital values may be peaking. The number of investors entering the forestry market reduced last year, in line with a growing confidence within alternative asset classes, such as equities and residential and commercial property. We predict that some of those who invested for the first time during the financial crisis may begin to exit the sector. Such private investors may seek to return to alternative asset classes where they may see opportunity for better returns in the short term.

As the wider economy improves and activity within the construction sector increases demand for timber, both as fuel and building material, can only grow. Traditionally, commercial woodland values were closely aligned to timber values but this link has weakened in recent years, with factors like renewables and tax benefits attracting new investors. However we expect this correlation to be restored as normality returns to the wider economy. We think that 2014 will be the year we start to see a recovering construction sector having a positive impact on timber prices, and that this in turn will have a knock-on effect on forestry over the next few years.

Despite any potential reduction in the number of investors, we are optimistic about timber prices. The significant tax advantages derived from commercial forestry, including the potential to benefit from significant IHT savings and Capital Gains Tax exemption, continues to point to a bright long term future for forestry.

As a leading rural property specialist, Savills handles the sale of commercial woodlands and advises on maximising returns from forestry investments throughout the UK. Savills rural team help farm, estate and forestry owners realise the potential of their assets through diversification into a wide range of activities including renewable energy, leisure and sporting pursuits.

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Summary

2013 has witnessed a record year both in the total value of the market and its unit price. During the year to September 2013 forest property (over 20 hectares and predominantly containing commercial conifers) to the value of £97.3 million was traded. This is 50% up on 2012 and 8.5 times the historically low value traded in 2000. The market has never been so active, particularly in Wales and interestingly, some 36% of UK sales this year were negotiated off market.

The average value per stocked hectare in 2013 is slightly up (2%) on 2012 at £7,057 per stocked hectare. This is the highest unit value we have recorded since we commenced this market report and annualised average growth since 2002 is now at 15.4%. This rise occurred despite a further recorded decline in timber price, as defined by the Forestry Commission’s standing timber price index which dropped 6.9% in the six months to March 2013.

This modest increase in average values is largely derived from investor optimism driving a strengthening market and less as a result of the type of properties traded in the year. Compared to 2012 a greater proportion of properties traded were of younger age classes <21 years old and with a tighter spread of Yield Classes (78% falling with Yield Class 12 to 16).

As ever, most of the sales (68.9% by value) were in Scotland. However, there has been a significant increase in recorded sales in Wales this year; 16% of the market compared to just 4% in 2012.

The number of properties traded in the year increased by 16% on 2012 with 79 transactions recorded and the area traded increasing to 13,780 stocked hectares, an increase of 47.3% on 2012 and the highest area recorded since 2009.

Average property size increased 27% to 174 hectares whilst the average property value rose 29% to £1,231,000 over four times the 2004 value. These averages are heavily influenced by the number of large sales in the year; 13 selling for over £2 million.

England no longer continues to command the highest price per hectare across all size classes. Indeed, the market in England has cooled significantly this year with the exception of one large sale to a special interest buyer. Last year we recorded English values exceeding £12,000 per hectare for properties greater than 50 hectares in size. This year, value has dropped below £10,000 per hectare. Furthermore, in Wales we have seen a number of larger properties (101 – 200 hectares) change hands at values exceeding £10,000 per hectare, outperforming their English counterparts in the same size range for the first time.

Last year, we recorded a shift away from the traditional negative correlation between property size and value per hectare. This year we see this trend continue, so whilst increasing age group and yield class continue to positively correlate with increasing value per hectare, investors appear to be taking a strategic view to large volumes of timber.

2013 has seen sale values continue to exceed guide prices by a weighted average of 14%, with the largest single property selling for 74% above guide price. In 2013, we have seen the appearance of a relationship between size and % over guide with smaller properties likely to sell for well over the guide and larger ones less so, although it should be noted that we have set guide prices for the private sales recorded at the sale price achieved. Transaction times have remained fairly constant compared with 2012 averaging 4.6 months from entering the market to completion.

Overall, the property market has maintained the strength we have seen build in recent years. Whilst the timber market to March 2013 has recorded a minor drop in value there is plenty of confidence in the market as Sterling remains weak against the Euro and domestic processors take advantage of this. The medium to long term looks promising as the wider economy starts to show signs of recovery, coupled with initiatives such as Grown In Britain promoting domestically grown timber to end users. This and the tangible benefits of land-based investments mean investors continue to show their confidence in the sector. All in all another headlining year for the forest property market.
It is important to remember that this report only focuses on properties over 20 hectares in size that are predominantly conifer. We also refer to individual years (2012 etc.) but the actual period each year covers is the beginning of October to the end of September in the following year.

**Total Market**

*Fig 1. Annual Total Value of Forest Area Sold*

- Figure 1 shows that the total value of commercial forest properties traded throughout England, Scotland and Wales (GB) has once again risen sharply. Market size for the year stands at £97.25 million, the highest value since 1998 and 50% up on 2012.
- This is 8.5 times the historically low value traded 13 years ago in 2000.

- Scotland still retains its position as the dominant player in the market, accounting for almost 69% of the total value traded, as illustrated in Figure 2. This is slightly down (5%) on last year due to a significant increase in market share for Wales. After a number of years of recording little activity in the Welsh market it is reassuring to see such an increase despite the impact of Phytophthora on the Welsh timber markets.

*Fig 2. Value of Market Share By Country*

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Market Analysis

Fig 3. Annual Sales: by Area and Number Sold

- Figure 3 shows that the area sold in 2013 is significantly up on 2012 by 47% to 13,780 hectares. This is the stocked area and not the total property area because all properties include a proportion of unproductive or non-commercial land; in 2013 we estimate this amounted to around an additional 19% of the area traded.

- Furthermore, the number of properties sold has increased to 79, an increase of 16% on 2012 and the highest recorded number since 2009.

- This substantial increase in area traded against only a moderate increase in number of properties traded has caused an increase in average property size in 2013 to 174 hectares, 27% up on 2012.

Fig 4. Annual Sales: Value of Average Sized Property

- This combination of significantly increased area and increased market size has pushed the average value of a property up 29% on 2012 values to £1,231,000, almost 2.5 times the 2010 value and seven times the 2002 value, as illustrated in Figure 4.

- Figure 5 shows that most of the transactions (34, equivalent to 43% of the total) related to properties with a value equal to or less than £500,000.

Fig 5: Frequency of Individual Transaction Size

- 18 properties sold for between £500,001 and £1 million, 14 between £1 million and £2 million and 13 properties sold for over £2 million.

- This is a far wider spread of property values traded this year than was seen in 2012.

- The 2013 data in Figure 6 shows value per stocked hectare at almost £7,100/hectare, only marginally up on 2012 (2%). This is the smallest jump we have seen since the report commenced.

Fig 6. Average Sale Price per Hectare and the FC Coniferous Standing Sales Index
• Looking back to 2002 the annualised average increase in property values per hectare has been 15.4%, an impressive result when compared with other asset classes.

• The Forestry Commission timber index for Great Britain is published twice a year and is derived from an analysis of data from every Forestry Commission sale over the preceding six month period. The index therefore reflects the timber market over the six months to 31 March and 30 September each year. The September data is not available until after this Report goes to press so the graph shows the largest annual value, i.e. the larger of the two data points within each year (using the Fisher 5 yearly nominal index) to illustrate the annual maximum.

• The Forestry Commission timber index actually decreased slightly from September 2012 to March 2013, dropping 6.8 points (6.9%) to 91.3.

• Notwithstanding this slight decrease it remains generally at a high point and we hold much confidence that it will rise again in 2014.

• Whereas historically we have seen a positive correlation between property values and the index we are now starting to see a departure from this trend. In 2012, the index was largely flat whilst in 2013 we have seen it drop. The same cannot be said for average values.

• Timber prices and the influences behind the standing coniferous timber sale market are discussed in detail in the UPM Timber Bulletin of Summer 2013 which also highlights the resilience of the UK timber industry in an otherwise turbulent economic environment.

• As was reported in 2012, in the property market we perceive a significant strengthening of interest, and allocation of value to more than just the current timber price, in particular;
  – The potential for log values to rise considerably in the medium to long term.
  – A potential shortfall in available timber volumes compared with expected demand levels, especially in relation to biomass where there seems to be enormous optimism.
  – An appreciation of woodland as an asset backed investment.
  – Increased values associated with land and infrastructure.
  – Increased values associated with non timber, ecological and carbon benefits.

• We see no reason to change this view; anecdotal evidence from timber sales recorded by us this year reflect a resource in strong demand from competing interests, with
particularly strong prices being paid by those seeking to secure processing and energy needs together.

- **Figure 7** shows that values per hectare vary by country and the size class of the property. For the first time we have seen England’s average values outperformed; Welsh values in the 101 – 200 hectare size class narrowly outperformed those in England. The Welsh properties in this category were largely mature forests.

- Otherwise, average values in England, across the remaining size classes, are highest, with this differential most notable in the smallest size category where, once again, they are more than double the Scottish value. This variation continues to be influenced by the higher underlying capital value and locational premium attributed to smaller English properties, especially in the south.

- **Figure 8** illustrates the continuing general trend of values per hectare increasing with increasing age.

- Values have generally remained flat or increased. The increases in mature forest prices paid is in stark contrast to the dip in timber price reported above.

- These transactions have been dominated by large properties, supporting our view that investors are nevertheless paying a premium for strategic reserves of timber, and a transaction in England purchased by a special interest buyer.

- **Figure 9** illustrates the relationship between yield class and average value per hectare. Yield class is a measure of average site productivity over the life of a crop, and is expressed in units of metres cubed of timber produced per hectare per year (m$^3$/hectare/year). The weighted average yield class in 2013 was 15, identical to that of 2012.

  - Higher yield class crops produce more timber in a shorter time than lower yield class crops and are therefore likely to produce more value per hectare (depending on timber quality factors and stocking density) over their life span.

  - The trend for higher values per hectare as yield class increases is clearly evident across the spread of yield classes, except for yield class 8, which shows much higher than expected values. The high value recorded for yield class 8 age 40+ is dominated by a single transaction in England with slow growing pines and a significant proportion of commercial broadleaf species.

  - **2013 saw a larger proportion of mid yield class (12 to 16) properties traded this year, some 12% more than 2012 and with a larger proportion in older age classes.**

  - **Notwithstanding this larger proportion in older age classes recorded values are up in some yield class categories and down in others.**
• Figure 10 shows that since 2006 the previous trend of larger properties recording a lower unit value has gradually ceased to be the case.

**Fig 10. Historical Values (£ per stocked hectare) by Size Class**

- 2007 saw a spike in the value of larger properties, mostly to do with some sizeable off market portfolio transactions of maturing, high yielding commercial properties.
- Through 2008 to 2011 the smaller properties (<50 hectares) jumped in value, largely because they are of an easily affordable transaction size for many investors and appeal to a wide range of investment interests.
- Over the last two years we have seen a dramatic increase in the values per hectare achieved for the largest properties (>101 hectares). 2012 saw the average price paid per hectare for properties >200 hectares leap above that of the smallest properties and although that has fallen back (down 9% on 2012) this year both they and the 101 to 200 hectare property (up 63% on 2012) size range command well in excess of the smallest size class.
- Indeed, this is the first year since 2007 that the average unit price of the whole transaction record has risen above that of the smallest size class.
- This further evidences our view that commercial investors continue to show a clear market preference and strong appetite to strategically acquire large volumes of timber.

• Figure 11 shows the relationship between the sale price and the property size, where the sale price is shown as a percentage of the guide price. Each transaction is shown as a data point and where the data point falls on the 100% line the property sold for the guide price.

**Fig 11. Sale Price as a % of Guide Price by Forest Size**

- It should be noted that for the purpose of this analysis we have set all off market, or private sale, guide prices to the selling price achieved, hence the subsequent concentration of data points at 100% (see discussion on private sales under Figure 12 below).
- Although some properties sell for less than the guide price (i.e. the data points positioned below the 100% line) most sell for more, usually less than 50% more but with some notably in excess of that with the largest % over guide being 74%.
- The weighted average is 14% over guide, which we attribute more to market strength and investor confidence rather than a tendency for agents to undervalue property. Guide prices are typically based on historical evidence, which quickly becomes out of date in a rising market.
- This year there does appear to be a relationship between the size of a property and the likelihood of it selling for significantly more than the guide price.

**Transaction Time**

- Woodland marketing and conveyancing always seem to take a long time, often a disproportionately long
time. This is not helped by the ever increasing legal burdens and risks inherent in the process.

- In 2011, we noted an average transaction period of 8.7 and were pleased to note this reduced to 4.8 months in 2012.
- In 2013, the recorded transaction time has dropped again to 4.6 months. This is largely due to the significant number of private sales recorded this year where buyers were professionally advised and transaction speed was integral to the sale negotiations; all bar one sale was completed within 3 months.
- It might be reasonable to assume an even split between the time spent marketing and agreeing a deal and the legal process.
- The three year average is 6 months, which suggests that purchasers could reasonably expect to allow up to six months to complete the purchase process. This can be highly significant to investors eager to commence the two year ownership clock to qualify for 100% Inheritance Tax relief.

Off-market Sales

- In 2012, we commented on a single substantial off-market sale in Scotland to a UK based investment fund. In 2013, we have recorded a substantial number of off-market or private sales that we have been involved in and are therefore included in this Report.

Timber Markets

The resilience of the timber industry through the recent turbulent economic environment has been a great achievement and despite the recorded dip in market prices this year we are convinced this will continue to be
the case. The weakness in sterling against the Euro is likely to continue for the foreseeable future meaning imported sawn timber remains relatively expensive.

In 2013, we have seen continued healthy demand for domestic timber and timber products fuelled by this reduction in imports of sawn timber as domestic processors have increased their market share. Total demand fell in 2012 but has now largely levelled off. During this time and in response to the Government’s Response to the Report of the Independent Panel on Forestry, the Grown in Britain initiative has been launched. One of its aims is to seek to promote the array of quality products generated from productive woodlands, and in so doing strengthening considerably the economic engine that underpins the forestry sector. The initiative has already secured long term commitments from over 30 UK companies in the retail, DIY, builder’s merchants, building contractors and building sectors to preferentially procure products from UK woodlands and forests. It is interesting to note that the total buying power of these companies is in excess of £50bn per annum.

In that light there is every chance that domestic processors will hang on to their increased share of the processing sector even if the Euro weakens because they offer a quality product with excellent service and lead times.

We commented above that some of the highest standing timber sale prices achieved this year were paid by processors seeking material both for processing and fuel for their energy needs. Woods and forests situated close to these markets stand to fair well when their timber comes to market in the future.

**Market background**

Most of the forests being traded today were originally planted between the 1960’s and the late 1980’s and contain predominantly Sitka spruce. The weighted average planting date of the 2013 data is once again 1978, making the average age 35 years old.

Individual properties were typically planted in one operation to create an even aged forest. Current forest regulations restrict extensive harvesting within a single property, which means that harvesting has to be undertaken in stages. This leads to greater age diversity within the property as mature crops are harvested and replaced with young crops.

Demand for timber has increased substantially in recent years as has the variety of products sought and derived from forests. The result is that investors not only appreciate the traditional timber production aspects of forests but also their wider credentials, for example, as a source of sustainable bio energy or as a green asset and a place to sequester carbon.

This research is a snapshot of the commercial forestry market in the year to September 2013. Woods sold in
previous years are therefore different from those analysed here. While these results show useful trends, readers should not base investment decisions on these comparisons alone and should always seek professional advice before committing to an investment.

Data collection
The UPM Tilhill and Savills Forest Market Report records some 1,288 transactions from October 1997 to September 2013.

• The properties are over 20 hectares in size and are predominantly conifer.
• Data includes crop ages and yield classes (estimated) for the primary productive species.

This report includes publicly recorded sales and, where possible, off market sales. Off market sales are difficult to quantify accurately due to their unpublicised nature and could add significantly to the total market value.

NOTE: The area referred to is not the gross total area but the stocked area, i.e. the net productive area which is carrying a crop. Unplanted land or ground for replanting is excluded. By analysing the stocked area we are focusing on the productive commercial elements of the properties in line with the overall intention of this report.

The transaction date used is that on which the legal liability is estimated to have transferred.

SEE THE WOOD AND THE TREES?
UPM Tilhill is always pleased to hear from anyone who is considering investing in forestry. We offer a full acquisition service and a seedling to harvester management service to help owners get the best from their forest regardless of size or location. If you would like to know more about how we may be able to help you buy, sell, manage or harvest timber, please contact one of UPM Tilhill’s Woodland Investment Advisers.

If you would prefer a virtual tour of a UPM forest, from the comfort of your desk, please visit the multi-award winning website www.upmforestlife.com.

While the forestry market is buoyant, large scale properties rarely come on to the open market as they often change hands privately. However, Savills, as a leading global real estate adviser, with specialists in rural property management across the UK, can keep you informed of opportunities as they arise.

Savills teams can advise on diversification, sporting, leisure and renewable energy opportunities provided by forestry. Forestry properties often offer renewable energy opportunities, particularly wind and hydro, and value is now almost always attached to such potential. Savills has a dedicated renewable energy team whose expertise includes site finding and assessment services.
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