



Savills World Research  
Rural

# Spotlight **UK Forestry Market**

2016



# Foreword

## INVESTING IN THE FORESTRY MARKET



UK forestry proved to be a strong performer in 2015 with a buoyant transactional market

**W**elcome to the second year of our joint research into the UK forestry investment market. Forestry remains a strong performer in land-based investments and early 2015 continued to show a buoyant transactional market for prime quality spruce forests in desirable locations. Over the period the total value traded was significantly more than in previous years at over £130 million worth of freehold sales and, despite this increase, our analysis shows further growth in the average value per hectare.

Prime investment forests focus on Sitka Spruce-dominated plantations mainly in upland areas. The rotation length is long, typically 35-55 years, therefore most investors only capture part of a growing cycle as opposed to the full process from planting to harvest. Continued capital appreciation coupled with annual biological growth of timber on a site has led to good investor returns over recent years.

Still considered by many to be a niche asset class, forestry investment offers multiple benefits and is particularly well suited to forming part of a balanced asset portfolio; it offers good long-term capital attributes, preservation through a benign tax regime and annual growth which, due to the method of valuation, treats the growing crop as part of the asset value.

The transactional market has not been even, with prime spruce dominated assets significantly outperforming more mixed conifer plantations, or indeed spruce forests in more marginal growing locations. The market performance of these more mixed assets was increasingly influenced by a slower timber trade, especially in the second half of 2015, when a strong Sterling/Euro exchange

rate created better conditions for imported timber, impacting on the competitiveness of domestic supplies. The best timber forests are more resilient to subtle movements in timber price, but where falling timber income is an important factor one of the key benefits of a crop that grows over an extended rotation comes into play, which is that there is no definitive harvest date. This means investors are able to alter harvesting plans (within reason) to smooth the impact of pricing changes, essentially banking value 'on the stump'.

As discussed last year, whatever the short-term fluctuations in price the link to timber is a key medium to long-term value driver as most commentators now agree that we will see structural shortages in global supply within a few decades. Control of a significant reserve of timber has therefore again been a key investment driver, and scale of investment does show positive benefits in this regard, with large funds and timber processors all keen to increase their strategic reserves.

New planting continues to hold significant opportunity and indeed as part of the possible response to widespread flooding is gaining increasing media coverage. It will be interesting to see how changing Government policy priorities may kick-start what was until the mid-1990s the primary entry into forest investment. ■



**Ralland Browne**  
Scottish Woodlands  
01738 625128  
ralland.browne  
@scottishwoodlands.co.uk



**Jonathan Henson**  
Savills  
01738 477511  
jhenson@savills.com

## EXECUTIVE SUMMARY



Value of investment forestry market has grown from £45m in 2010 to £137m in 2015  
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Recent research shows a continuation of the general upward trend in average plantation values  
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Timber prices experienced a slowdown in 2015  
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The popularity of amenity woodlands continues to increase  
See page 09



The outlook for the forestry investment market in the longer term remains positive  
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### This publication

This document was published in March 2016. The data used in the charts and tables is the latest available at the time of going to press. Sources are included for all the charts. We have used a standard set of notes and abbreviations throughout the document

# FOREST INVESTMENT ANALYSIS

The overall volume of forestry transactions increased in 2015 to nearly 21,000 hectares

**O**ur Spotlight on the UK Forestry Market 2016 reviews the performance of the investment forestry market across Great Britain during the 2015 forest year (1 October 2014 to 30 September 2015).

Our research is based on our transactional database of forest sales. This database collates data from all mainstream forest sales, and where we are aware, off-market or private transactions.

Our analysis shows that the overall volume of forestry transactions grew by about 30% to nearly 21,000 hectares in 2015 compared with just over 16,000 in 2014. This follows a period where the area of forestry sold has been fairly constant at around 16,000 hectares a year (Figure 1).

This rise in the number of hectares sold in 2015 is predominately due to a significant number of off-market sales, which in the 2015 forest year

included a portfolio of 16 properties sold by UPM to the Church Commissioners for around £50 million, as well as the disposal of two smaller investment portfolios.

The total area of land sold within these transactions makes up a third of all sales recorded during the year and cannot be classed as 'normal' market activity. Adjusting for these portfolios the overall traded area is probably slightly lower than the recent average.

Our research splits the investment forestry market into four key regions:

1. North Scotland
2. Central Scotland
3. South Scotland
4. England and Wales

The 2015 data shows a significant increase in the proportion of land sold in South Scotland (Figure 2), which is largely influenced by the location of properties included in portfolio sales; for instance in the UPM portfolio over three quarters of the total area was located in South Scotland. England and Wales continues to show the smallest average market share by region.

### Total market value

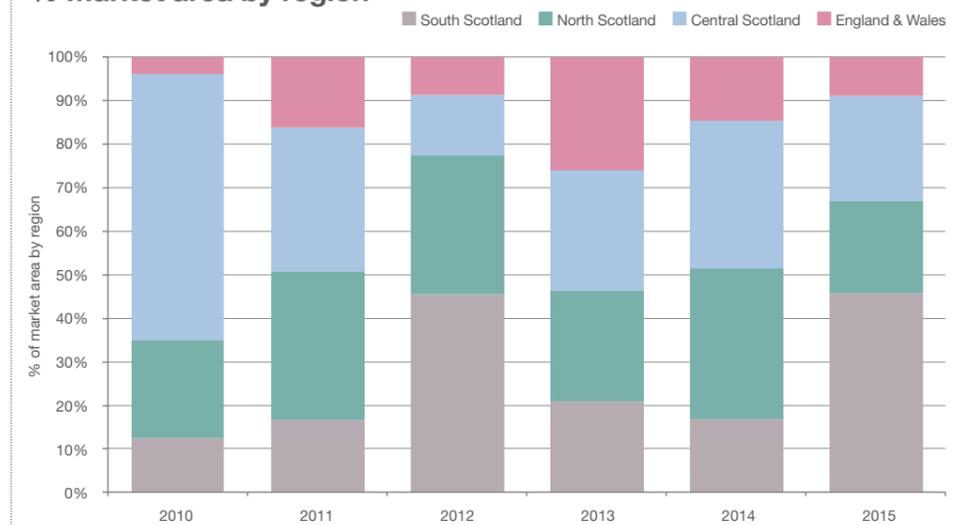
Over the last five years, the cumulative value of the investment forestry market has shown marked growth from around £45 million in 2010 to £137 million in 2015 (see Figure 3).

As would be expected, the increased market area in 2015 has been reflected by a substantial rise of over 60% in the total value of the market compared however, to the previous year. It should be noted that portfolio sales are not annual events and adjusting the data for these would bring the total value of the market more in line with the five year average of £72 million.



FIGURE 2

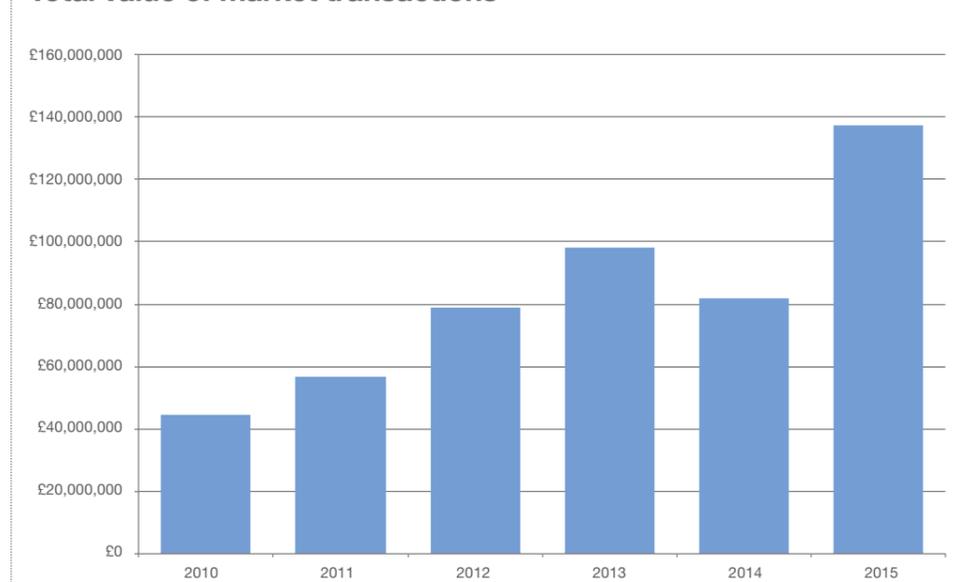
### % Market area by region



Source: Scottish Woodlands and Savills Research

FIGURE 3

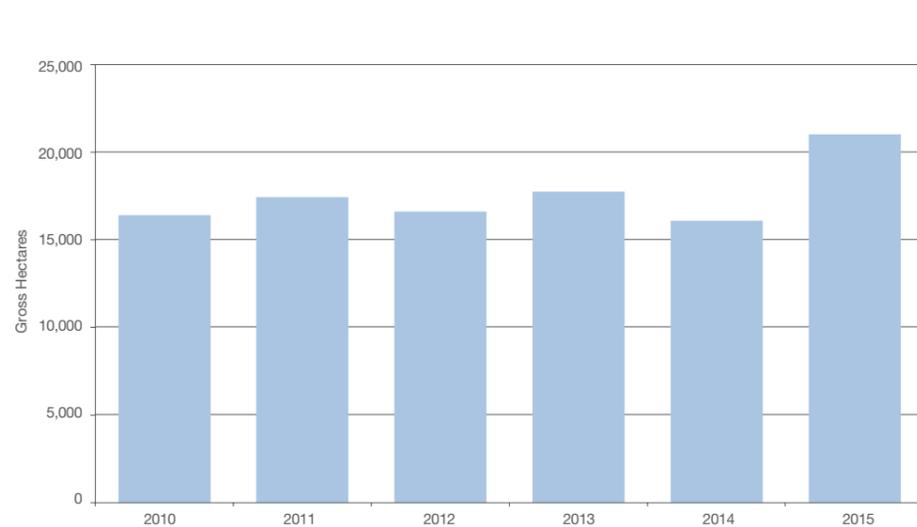
### Total value of market transactions



Source: Scottish Woodlands and Savills Research

FIGURE 1

### Total market area



Source: Scottish Woodlands and Savills Research

**21k**  
Number of gross hectares sold in forest sales in 2015

**£137m**  
The cumulative value of the forestry investment market in 2015

#### Methodology

While every effort is taken to ensure all transactions are included within the information presented in this publication, full information is not always available and information on some transactions only becomes known following the launch of previous research publications. Therefore where appropriate historic data previously reported in our Spotlight on the UK Forestry Market 2015 has been updated to take account of new information now available within the marketplace.

→ **Average values**

Our recent research shows a continuation of the general upward trend in average plantation values (Figure 4).

As with the agricultural land market, average forestry values are diverse, and factors such as location, quality, access, timber species and plantation age all have a bearing on the price paid.

According to our analysis of the 2015 sales data, the average value

per productive hectare [measured as the land area of a property stocked with trees capable of producing an end crop of timber] rose by 13.5% during the 2015 forest year to £8,615 per hectare. This is 21% higher than the average gross value [total property area] at £7,118 per hectare. The annualised rate of value growth over the past five years (2010-2015) was similar for net productive hectare and gross hectare at 16% and 17% respectively.

A wider gap between gross and net price tends to correlate to periods of stronger market competition. The value per productive hectare tends to track timber price more closely as illustrated in Figure 4, where between 2012 and 2014 the productive area value levelled out before rising steeply between 2014 and mid-2015, when timber prices were strong.

**Regional performance**

As reported in our 2015 Spotlight on the Forestry Investment Market the highest values continue to be achieved within the South Scotland region and then across England and Wales (Figure 5).

This correlates to the importance of South Scotland and the Borders area to timber production and also the general scarcity of forest property transactions in England and Wales, leading to a slightly different pricing structure.

Our research on regional performance by value and age illustrates how forest values increase with age, driven by the accumulating stock of available timber and the reducing time until income realisation.

It is interesting to note that the value of younger forests in England and Wales has increased significantly from around £4,500 per hectare in our 2014 analysis to £6,500 per hectare, without a commensurate increase to the value of older property in this region, therefore flattening the price-age profile.

In our research we have looked at regional market trends. Figure 6 shows the percentage difference between the gross property area and the net productive area of property traded in the four analysis regions.

It can be seen that there is a smaller gap between the gross and net productive area in England and Wales with the widest gap in North Scotland. Our research into gross

and net values indicates that there is a fairly consistent gap between the gross and net values but with a change in rank in average price observed between net and gross; South Scotland is the top performing region based on net productive area, but England and Wales is the top performing region on average price per gross area.

This reflects the different nature of property between the regions with many woods in England and Wales stocked from 'fence to fence' with little open space beyond rides and roads.

Furthermore, the smaller nature of the market in England and Wales means that scarcity and competition for property are also likely to accelerate values above those supported by pure timber economics, whereas in South Scotland, productive capacity is a primary driver of value.

**Timber prices**

The Forestry Commission's Timber Price Indices for Coniferous Standing Sales (Figure 7) published in November 2015 shows that there has been an overall increase in the index over the last 12 years, following an overall decrease in earlier years. The index was 1.2% higher in real terms in the year to September 2015, compared with the previous year.

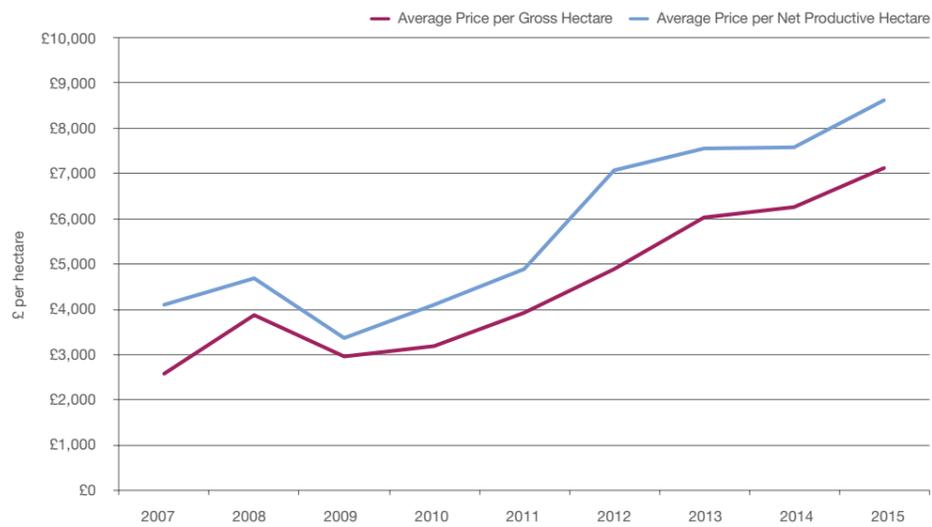
However, these figures mask the slowdown in the timber market experienced over 2015 when the sawn softwood/sawlog market finally lost momentum after almost twelve months of continuous upwards price movement. The influence of price pressure exerted by sawn timber imports became increasingly evident throughout the year and domestic carcassing prices fell by over 10%. The wood-based panels sector benefited from the increase in new house building but it was not immune

from the strength of sterling and the effect of the lower price of imports combined with overproduction of certain categories in Europe. Over the period the average value of sawlogs dropped by 6% but the average price of small roundwood remained unchanged. The stability in the small roundwood market was undoubtedly underpinned by the demand from the biomass energy producers and the wood-based panel manufacturers.

The main influence in the downward price pressure on the timber market is currency. During the analysis period the pound strengthened against the Euro by around 8% and Swedish Krona (Figure 8) by about 10%.

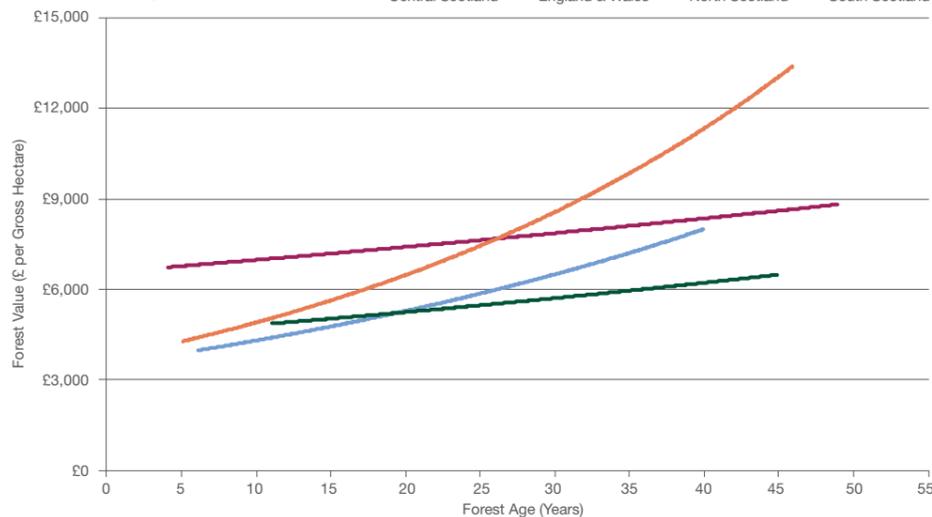
This allowed imports of sawn timber to undercut domestic producers leading to a reduction in demand for home grown construction timber. This not only impacted sawn

FIGURE 4 Average sale price



Source: Scottish Woodlands and Savills Research

FIGURE 5 Regional Performance The relationship between forest age and value by region

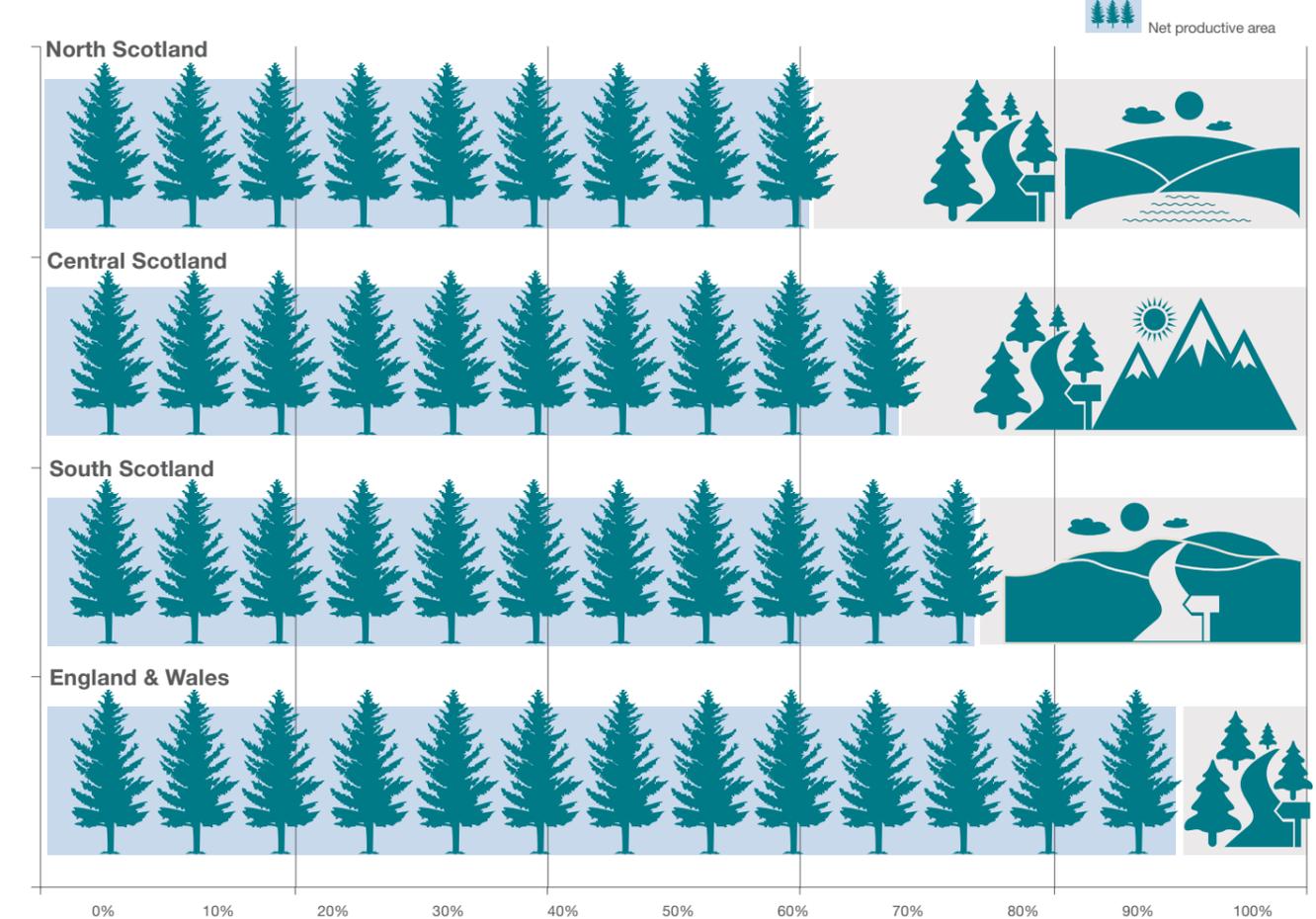


Source: Scottish Woodlands and Savills Research



Average value per productive hectare in 2015 rose to £8,615

FIGURE 6 Average productive area by region

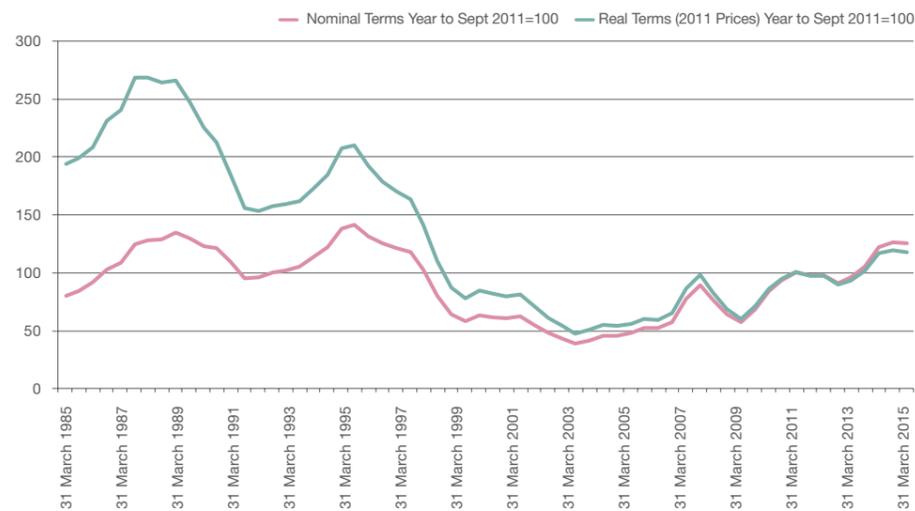


Source: Scottish Woodlands and Savills Research

→ timber imports, but also on our competitiveness with timber product exports including paper. Growers have benefited from the long period of strong demand and high prices but 2015 was a more difficult year for timber values. There has been a need to rebase prices for logs and standing timber to reflect the impact of imports whilst the exchange rate is unfavourable. There are [Winter 2015] fresh indicators of a weakening in Sterling around discussion on a possible BREXIT and there are also signs that

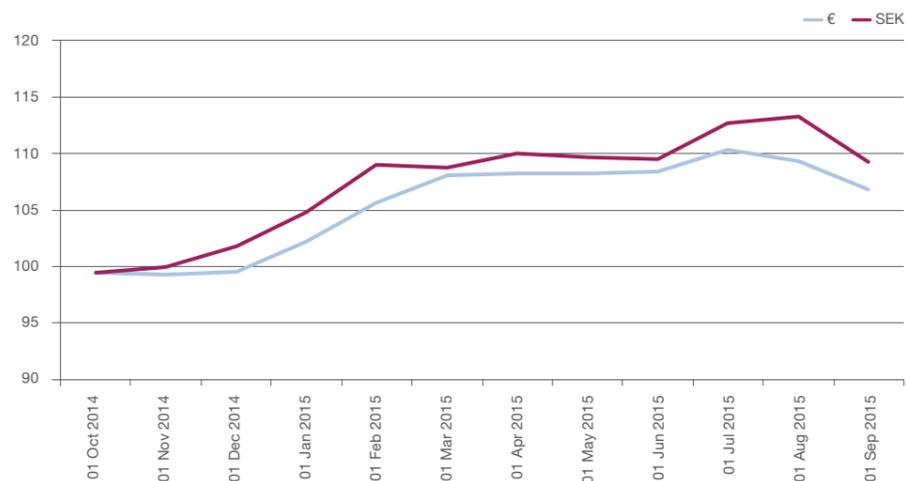
some of the most important EU industrial economies are recovering which should strengthen the Euro in the medium term. In addition there is a still healthy demand for wood products. Despite the current downturn in the price processors are able to pay for logs, the demand for standing sales (especially of certified timber) will increase as we move further into 2016 and sawmill stocks are increased to supply increasing demand for construction timber. This should help strengthen roundwood prices. ■

FIGURE 7 Forestry Commission Coniferous Standing Sales Index (long term)



Source: Forestry Commission

FIGURE 8 Value of Sterling against the Euro and Swedish Krona



Source: The Bank of England & Savills Research

## FULL VALUE Marketing woodland

The UK forestry market has recently been dominated by a small number of very active buyers, but wider interest in forestry as an investment is increasing. Active and appropriate marketing of forests continues to attract new buyers into commercial forestry, which can only be a good thing for sellers, and for the wider industry.

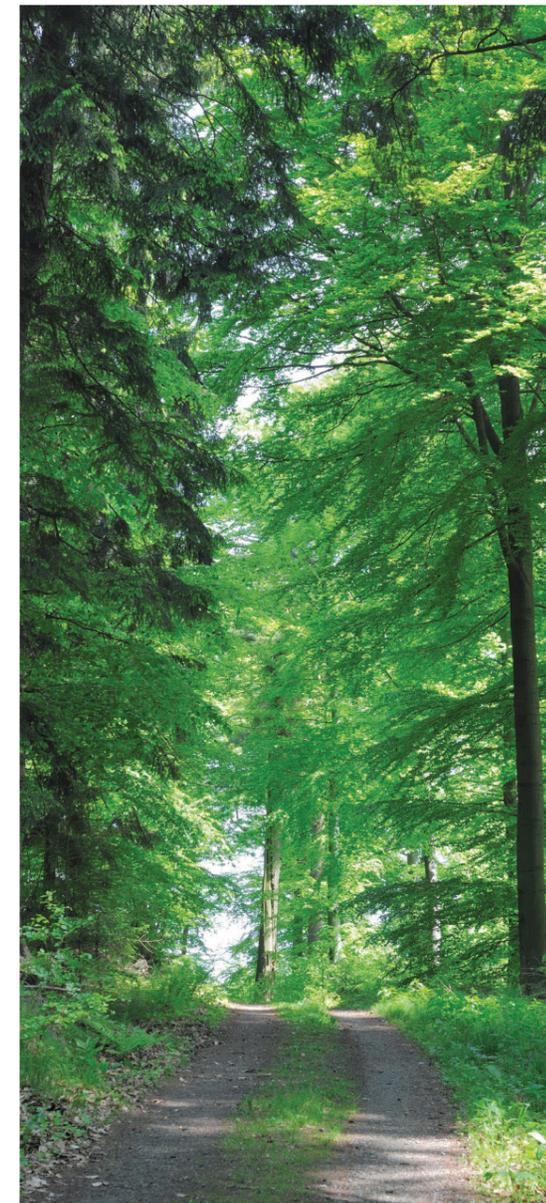
For those contemplating a sale, presenting the property well and resolving any outstanding issues prior to marketing is essential. Purchasing solicitors are now forensic in their approach, and unforeseen issues which lead to a delay in progressing a sale can put the whole sale in jeopardy. The title boundaries and physical boundaries of forestry properties are notorious for not marrying up. Resolve these prior to marketing, as trying to do so after an offer has been accepted will result in significant delays and potentially deals falling through.

The primary focus of forestry investors will be on the timber crop. Ensure crop records and compartment plans are accurate and up to date. By making these accurate, purchasers will be reassured, and importantly the full stocked area of the forest will be used when they come to analyse the level of their offer.

Finally, first impressions do count, even for commercial forestry. If a forest looks well managed purchasers will assume that it is well managed. This can be achieved by ensuring that gates swing freely, internal tracks are passable, and where feasible areas of windblow are cleared prior to marketing. A period of modest expenditure prior to marketing may reap great rewards when it comes to receiving offers.

# INTO THE WOODS

Landowners who have small pockets of woodland they can't find a use for may find a market in the amenity woodland owner



**A**menity woodlands are one of nature's playgrounds. They don't have a huge commercial value in terms of timber, yet they are highly desirable as places to go for recreation and enjoyment and many people want a small piece of woodland to call their own. Amenity woods are usually small parcels of land, anything from two to 20 hectares, that are visually appealing and normally close to where the owner lives.

The greatest demand is in southern England and the Midlands near big urban conurbations and in the right location values can reach £10,000-£15,000 per hectare. Value is however not simply measured in price per hectare, but more the 'affordability' of the total price, which can lead to some very high looking unit prices.

Over the last 20 years, the popularity of amenity woodlands has steadily increased. Generally, these are small fragmented blocks in lowland areas. Quite often they are a headache from an estate management point of view, but highly desirable to someone who wants woodland for recreation or to add value to a house. For amenity

woodlands to be as attractive as possible to buyers, they should have a good visual landscape, a mix of trees, have good access off a county road and be well managed.

A buyer's main motivation is usually for a sustainable piece of land that promotes wildlife and is good for recreation. However, it is rare that there is no commercial value at all and owners should be able to produce enough firewood for their needs – or even to turn a small profit. Once you have 10 or 20 hectares there's always an element of timber and the firewood market is very strong. A lot of people have installed woodburners, so there is a continuing demand and because firewood is a lower quality resource, it tends to come from under-managed woodland.

While amenity woodlands were a strong investment 20 years ago, when their initial costs were cheaper, the market has changed and you may not see a lot of capital appreciation. However, commercially managed woodland of any type should attract Business Property Relief from Inheritance Tax so these purchases can still be made tax efficient. ■

## TAX BENEFITS

### An efficient investment

Commercial forestry has long been seen as a tax-efficient investment, with the fiscal policies of successive British governments since the 1980s having a greater influence on woodland values than timber prices. Income Tax relief on forestry planting expenditure in the 1980s fuelled investment in woodland creation, whilst shelter from Inheritance Tax has been of primary importance since the 1990s.

The tax benefits of commercial forestry remain. Income generated from the sale of timber is exempt from Income Tax and Corporation Tax, making forestry an effective means of converting capital into tax free income. Commercial forestry also qualifies for 100% Business Property Relief once held for two years, so that if held at death there is no Inheritance Tax payable on the total value of the land and the trees.

## OUTLOOK

### The prospect of a longer term upward trend remains very real

Our Spotlight analysis has shown another year of growth measured both on gross or net property area, at 14% and 13.5% respectively, a trend first identified in the late 1990s. One question often asked is where does the end of this strong bull-run in forest values lie? The answer is of course anybody's guess, but reasoned analysis of the fundamental drivers of forest investment suggests there is still some way to go.

We are undoubtedly moving into an era where forest values will be increasingly influenced by the productive capacity of the asset, or put simply the value of the stock of available timber on a site adjusted for the time to realisation. High yield class, well managed commercial spruce forests with good access to timber markets will remain in strong demand unless something fundamental changes. Younger forests or land for new planting of commercial conifers will also prove interesting. The primary driver here is the expectation of a seismic shift in timber prices over a longer timeframe, perhaps 20 to 30 years.

There is however some polarisation apparent in the market and as we moved through 2015 any forest property offered for sale that did not tick all of the normal investment criteria showed signs of sticking on the market unless competitively priced.

The effect of this is likely to feed into next year's market analysis. Value investors may see a softening as an opportunity to step into the market for more mixed conifer assets with a view to longer term improvement in a subsequent timber rotation; others will no doubt wait and see what transpires over the next year or two.

But forestry is not a short-term game and as an asset class we normally recommend a minimum 10-year investment horizon. Looking further forward, strong growth in the demand for wood fibre (biomass), upscaling in the demand for wood for use in construction (both sawmilled and processed timber),

regionalisation of global supply-demand flows and the ability for an increasing world population to provide ready markets for excess capacity will all contribute towards wood being a sought-after commodity.

Although UK timber markets will fluctuate from season-to-season and year-to-year, the prospect of a longer term upward trend in timber pricing structures remains very real, making us confident in the future of forestry as an asset.

Finally, we are entering a period of intense debate about the EU Referendum and what the outcome may or may not mean for the UK. At this stage the potential implications for timber, forestry and investment in the sector are too unclear to comment on with any authority. What we do know, however, is forestry has in the past shown excellent resilience in times of uncertainty, underpinned by its long-term nature and link to a valuable commodity.

## Rural Research

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## About Scottish Woodlands

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Scottish Woodlands Ltd is a leading forest services provider with a long tradition of serving forest owners and investors in Scotland and the rest of the UK. Founded 75 years ago we are client and customer focused and operate to the highest standards of safety and environmental awareness. We actively manage around 150,000 hectares of forestry and in 2015 harvested and marketed 1 million tonnes of client timber. The Company operates from a network of 17 offices around the UK.



## Meet the teams

### Savills

### Scottish Woodlands



**Jonathan Henson**  
Director  
01738 477511  
jhenson@savills.com



**Alastair Gemmell**  
Director  
01738 477520  
agemmell@savills.com



**Ian Bailey**  
Head of Rural  
Research  
01797 230156  
ibailey@savills.com



**Nicola Buckingham**  
Research Analyst  
01398 332170  
nbuckingham@savills.com



**Ralland Browne**  
Managing Director  
01738 625128  
ralland.browne@scottishwoodlands.co.uk



**James Adamson**  
Investment & Business  
Development Manager  
01738 474082  
james.adamson@scottishwoodlands.co.uk



**Marc Liebrecht**  
Director  
01543 261999  
mliebrecht@savills.com



**Andy Greathead**  
Director  
01620 828979  
agreathead@savills.com

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33 Margaret Street  
London W1G 0JD  
020 7499 8644

[savills.co.uk](http://savills.co.uk)

