

F&W FORESTRY LETTER



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SPRING 2006

Dry Weather Brings Price Declines Across All Timber Products



By Marshall Thomas

An early start to the dry weather usually associated with the beginning of summer was the probable cause for timber price declines across all species and products during the first quarter of 2006 (see weather map, page 4).

Hardwood pulpwood led the decline with a price drop of 13%, or a little over

\$1/ton, during the three-month period ending March 31. Hardwood sawtimber, however, remained fairly stable registering a decline of just 2%. Pine products declined, respectively, 2%, 7%, and 6% for pulpwood, small sawtimber, and large sawtimber.

These are probably normal seasonal trends. Unfortunately for timber sellers, the normal annual downturn associated with dry weather began a little earlier than "normal" this year. I say earlier than

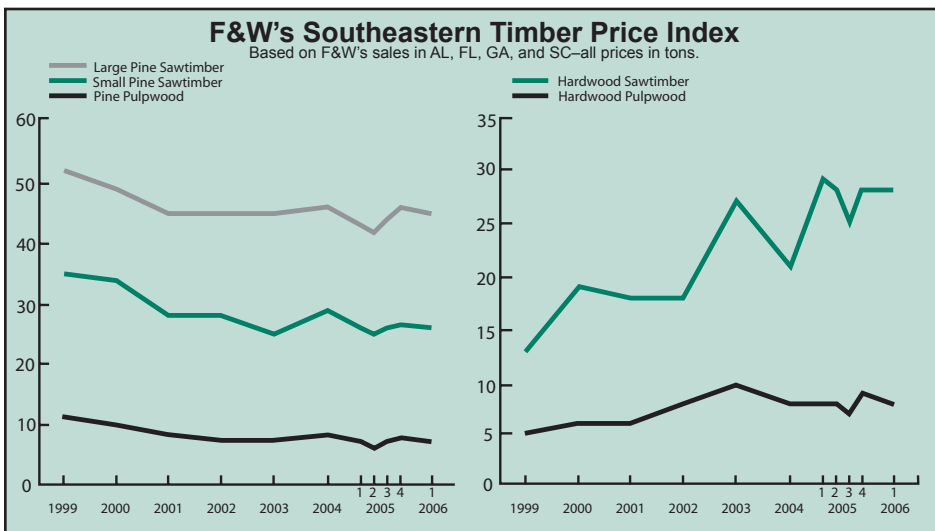
Inside This Issue

There's much "must" reading inside this F&W Forestry Letter. A comprehensive report on International Paper's close-out forestland sales along with a disturbing new survey of Southern tree planting, pages 2 & 3. U.S. and Canadian government heads aim to restart lumber import talks, and Canada's largest forest company establishes a beachhead in the South, pages 4 and 5.

"normal" when compared to long-term trends. However, based on the last five years or so, 2006 seems to be shaping up as pretty normal and dry.

It is interesting that lumber mills have been able to keep the prices they pay for pine sawtimber as stable as they have, given the strong increase in Southern pine lumber prices that has occurred since 2003 (from \$311/mbf to \$393/mbf, see Southern Timber Market Indicators, page 6). We have to keep in mind that the mills were probably losing money in the early part of this decade, but you would think that some portion of an increase of over 26% in lumber prices would have made its way to the landowner by now.

While there is a lot of concern about trends in the housing market, the fact is that a whole lot of new houses are still being built—certainly enough to sustain current lumber price levels. I think we need a long period of very wet weather to find out just how much of the lumber price increases can be passed along to the landowner without forcing the mills into the red. I certainly am not hoping for any more hurricanes, but three or four strong and wet tropical storms over the summer and into the fall might bring some cooler weather and a hotter market for Southern landowners later this year and in early 2007. ■



2006 First Quarter Pine Stumpage Price Range*

Area	Pulpwood (Tons)	Small Sawtimber (Tons)	Large Sawtimber (Tons)	Large Sawtimber (MBF)
Phenix City, AL	\$6-8	\$23-27	\$42-54	\$280-375(S)
El Dorado, AR	\$4-9	\$18-23	\$45-49	\$320-330(S)
Gainesville, FL	\$6-10	\$25-30	\$42-49	\$294-343(S)
Marianna, FL	\$7-9	\$20-28	\$38-43	\$297-337(S)
Albany, GA	\$7-9	\$23-25	\$48-55	\$312-358(S)
Macon, GA	\$5-8	\$23-31	\$45-53	\$315-371(S)
Statesboro, GA	\$8-11	\$25-32	\$38-55	\$275-375(S)
Jackson, MS	\$3-6	\$15-20	\$38-55	\$275-380(S)
Greenwood, SC	\$8-10	\$22-24	\$45-48	\$315-350(S)
Huntsville, TX	\$3-5	\$16-18	\$33-41	\$247-304(S)
Charlottesville, VA	\$6-10	\$20-26	\$30-42	\$180-250(I)**

*Based on sales handled by F&W offices. If no sales occurred, prior quarter's sales and other data are used to compile price range.

Price ranges are due to different locations, timber quality, logging conditions, type of harvest, and local market conditions.

To convert \$/ton to \$/cord multiply \$/ton price by 2.7.

The actual range for our sales, depending on region, is from 2.6 to 2.8.

**Virginia Pine Sawtimber is \$90-100 MBF (I). (S) = Scribner (I) = International

Marshall Thomas is president of F&W Forestry Services, Inc.

IP Completes Historic Land Spin-Off; Keeps Supply Rights

In a series of sweeping transactions that add up to the largest sale of forestland in U.S. history, **International Paper Co.** has completed the divestiture of 5.7 million acres—mostly in the South—to private investors and conservation groups for an overall average price of just under \$1,160 an acre.

IP said it will retain contract rights to draw about 20 percent of the wood and fiber needs of its mills from the divested lands over the next 10 to 50 years at “market prices” to the new owners. The lands must continue to be managed according to sustainable standards.

When the sales are completed—probably by the end of this year — IP’s land base in the U.S. will have been reduced from more than 8 million acres a few years ago to 830,000 acres. That’s about one-tenth the holdings of the nation’s new undisputed forestland giant, **Plum Creek Timber Co.**, based in Seattle, Wash. Plum Creek became a major player in Southern timberlands largely through its purchase of **Georgia-Pacific’s** woodlands in 2001.

IP’s corporate coffers will be enriched by almost \$6.6 billion by the land sales (before taxes), half of which will eventually be used to pay down debt, according to the company.

The sales were announced over a two-week period in late March and early April that transformed forestland ownership in the South. In the period before and after World War II, pulp and paper companies bought up millions of acres of Southern lands, much of them agricultural, to grow wood fiber for their mills that sprang up across the region.

Today, not counting International Paper’s drastically reduced holdings, only three paper companies maintain

sizeable forestland bases in the region: **MeadWestvaco**, **Temple-Inland**, and **Rayonier**.

IP said the spate of timberland sales, concluding with 275,000 acres in upstate New York, substantially completes the land-sale phase of the massive transformation plan it announced last July. Still in play are the sale or spin-off of other operations targeted in the reorganization plan,

land: 3.8 million acres across the South and 440,000 acres in Michigan for approximately \$5 billion. TimberStar agreed to buy 900,000 acres in Arkansas, Louisiana, and Texas for \$1.1 billion. Both deals were for cash and notes, according to IP.

The two conservation groups agreed to buy 218,000 acres of ecologically sensitive forestlands, clustered largely around rivers and estuaries, in 10 Southern states for \$300 million. The Nature Conservancy bought another 69,000 acres in Wisconsin for \$83 million.

With all buyers, IP negotiated agreements to supply wood and fiber to its pulp, paper, and wood product mills. For the private sector buyers, these agreements would extend for a period ranging from 10 to 50 years with IP paying, in the words of the announcement, “market prices” for the timber.

“We are very pleased with the terms of both agreements [RMS and TimberStar], which allow us to capture about 20 percent of our annual softwood fiber requirement from these lands for our pulp and paper facilities, which is only slightly lower than our historic levels,” said David Liebetreu, IP’s vice president for forest resources.

The separate announcement of the land sales to the Nature Conservancy and the Conservation Fund was less explicit about the wood/fiber supply agreement. It said the majority acreage would remain in “working forests” and that timber would be “sustainable harvested” from some tracts, with a “set amount” supplied to local IP mills.

IP said 1,300 foresters and other employees currently are involved in managing the lands being sold. Some will continue in this capacity under the new ownerships. ■

Shrunkn Giant: IP Forestland Ownership In South Before And After Close-Out Sales

State	Acres Before	Acres After	Percentage Retained
Alabama	1,200,000	120,000	10%
Arkansas	690,000	70,000	10%
Florida	240,000	40,000	17%
Georgia	570,000	130,000	23%
Louisiana	650,000	70,000	11%
Mississippi	400,000	30,000	8%
North Carolina	630,000	130,000	21%
South Carolina	630,000	80,000	13%
Tennessee	200,000	500	.25%
Texas	650,000	30,000	5%
Virginia	190,000	25,000	13%
Total	6,050,000	725,500	12%

Source: IP Media Relations Office. Acreages rounded; includes Blue Sky Properties.

including the company’s expansive wood products business—lumber, plywood, poles, OSB, and engineered wood—again located largely in the South.

A transfigured International Paper, which is relocating its corporate headquarters to Memphis, will focus on two pulp and paper industry segments: uncoated papers and consumer packaging.

Except for the New York sale, buyers of IP’s forestlands are two separate private investor groups led by **Resource Management Service, LLC (RMS)** of Birmingham, Ala., and **TimberStar** of Atlanta. The two national conservation groups are **The Nature Conservancy** and **The Conservation Fund**. Buyer of the upstate New York land is **Lyme Timber Company**, a New Hampshire firm.

RMS got the biggest chunk of IP

Southern Tree Planting Declines Again In 2005

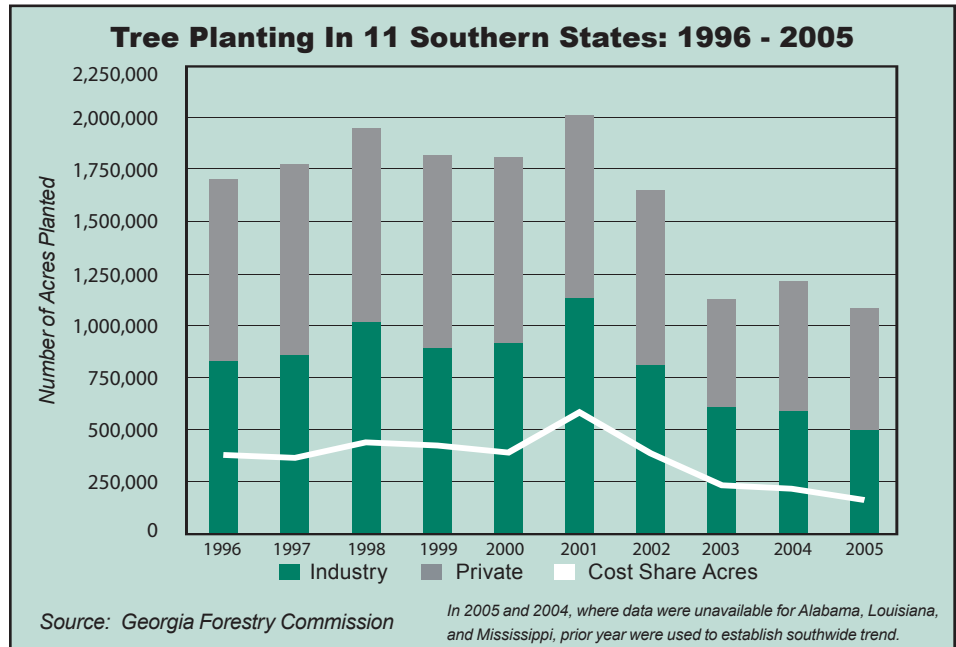
Tree planting across the South plunged 12 percent in 2005. It was the smallest number of acres to be planted in the region in a quarter century.

About a million acres of pine seedlings were put in the ground during the 2005 planting season—the winter of 2004-05—a decline from 1.2 million acres from the prior year and about half the peak years of the Conservation Reserve Program of 1985-90.

The most recent year that Southern tree planting shrank as low as a million acres was 1981.

Tree-planting statistics for the 11 Southern states, plus Oklahoma and Kentucky, are compiled annually by the Georgia Forestry Commission, a state agency, from data assembled by its sister state forestry agencies. The data are drawn from tree nursery production figures, forest industry information, and other sources. They include both pine and hardwood plantings, with pine species accounting for 90 to 95 percent of the total in most years.

The latest survey leaves no doubt that Southern tree planting has firmed into a downward trend that began in 2002. That year, 1.8 million acres were planted in the 11-state region



by private, non-industrial landowners and the forest industry—a decline of 428,514 acres from 2001. The number of planted acres has decreased every year except one since.

The decline has occurred on both private, non-industrial lands and on forest industry lands. The drop off in tree planting by the forestry industry became notably sharper in 2003, about the time a number of pulp and paper companies began selling off their timberlands.

Southern forestry authorities are unsure what the continued slump in tree planting means now or for the future. Depressed stumpage prices received by landowners are frequently cited as a deterrent to tree planting, but timber prices have shown modest improvement in recent periods and the decline has continued.

Another oft-noted factor in fewer tree-planted acres is the sharp reduction in financial incentives provided by government agencies—especially federal agriculture and forestry cost-sharing programs like the Conservation Reserve (CRP) and Forest Incentives (FIP) programs. Many of these programs have had their funding sharply reduced by Congress

and the Administration or abolished entirely.

These funding cutbacks appear to be a significant factor in the decline in tree planting. According to the Georgia Commission survey, the number of non-industrial acres planted to trees with federal or state financial assistance has dropped from 844,700 in the peak CRP year of 1989 to just 179,926 acres in 2005. The percentage of government-subsidized tree planting on privately-owned lands dropped from 73 percent in 1989 to 38 percent in the most recent years.

While the Georgia survey monitors the estimated number of tree acres planted, it does not seek to measure annual growth or volume. That is the role of on-going surveys conducted by the U.S. Forest Service. It is reasonable to assume, however, that forest productivity may be increasing as the planted base declines as a result of advances in silviculture, including greater use by tree farmers of herbicides, fertilizer, and other intensive management practices to enhance per-acre volume growth.

In other words, going forward, the South may be growing more wood on fewer acres. ■

Paper Recycling Hits Record

Even as tree-planting in the Southern wood basket continued to decline, paper recycling in the U.S. hit a new record in 2005. According to the American Forest & Paper Association, 51.5 percent of the paper consumed by Americans last year was made from recycled fiber.

AF&PA said paper recycling has increased 76 percent since 1990 when the paper industry launched a recovery program. Currently, Americans recover approximately 346 pounds of paper per capita, up from 233 pounds in 1990. The industry has a goal of 55 percent recovery by 2012. ■



Canadian Forestry Giant Invades South; Buys S.C. Company

Canfor Corporation, a leading Canadian forest products company, has agreed to buy **New South Companies, Inc.**, based in Myrtle Beach, S.C., with extensive lumber-related operations in North and South Carolina, in a deal valued at \$205 million.

The acquisition of New South marked the first entrance of the Vancouver-based forestry giant into the U.S. South and follows other Canadian moves into the OSB segment of the Southern forestry industry. It may not be the last Southern move for Canfor.

New South operates three sawmills, two treating plants, a finger joint plant, and a European lumber import business with annual sales of about \$500 million.

Canfor is Canada's largest producer of softwood lumber and a major producer of pulp and paper, oriented strand board, and other products.

Canfor President Jim Shepherd said his company is committed to a vigorous growth strategy. "When you have all your eggs in one basket, meaning here in B.C. (British Columbia), we're subjected to all the risks that go with that," he told Canadian media in connection with the New South acquisition. "There's timber pricing, there's the softwood lumber deal, there's the currency risk, there's all these things. Part of our motive here is to broaden our geographic diversity, mitigate the risk somewhat, and provide the products our customers are looking for."

Shepherd has also expressed interest in the lumber and OSB businesses **International Paper** is considering selling as part of its massive restructuring plan announced last summer. "We have every intention of moving into the United States with acquisitions or growth opportunities in the U.S. and we will be very aggressive in looking into those opportunities," he said at the time.

Separately, **Shuqualak Lumber Co.** of Shuqualak, Miss., is moving forward with previously published plans to build a \$140 million laminated engineered wood plant at Meridian, Miss., near the border with Alabama. ■

MeadWestvaco Enhances Its Southern Links

MeadWestvaco Corporation, currently based in Stamford, Conn., is the latest pulp and paper company to abandon the Northeast for the South as its base of operations—choosing Richmond, Va., for its corporate headquarters. It will also establish a new research center in Raleigh, N.C.

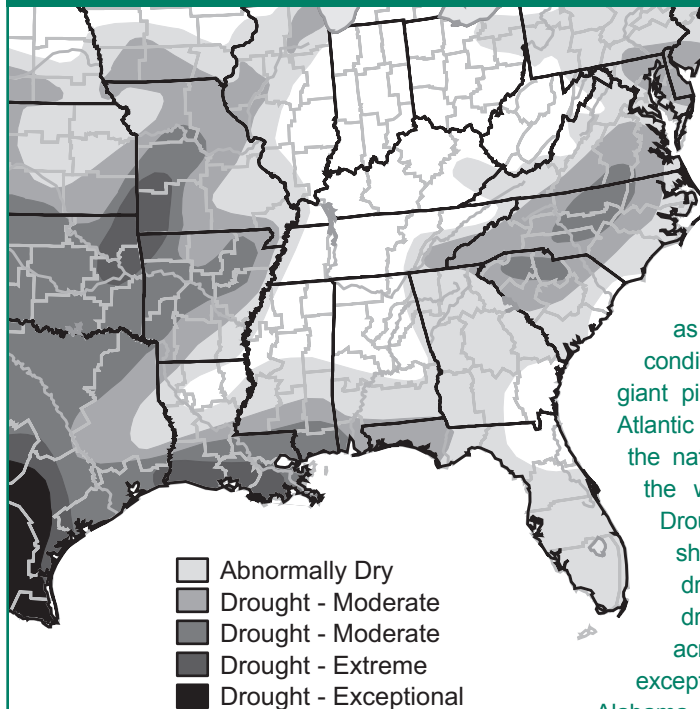
The company will lease temporary space in the Virginia capital city this summer before moving to permanent headquarters somewhere in the metropolitan area in 2008. One branch of the company—Westvaco—was founded in West Virginia in 1888. It established a presence in its new home state in 1900 with a paperboard mill at Covington in the Allegheny Mountains, which is still in production. The other part of the

company—Mead—has its roots in Ohio.

Other pulp and paper companies that have recently relocated their corporate headquarters to Southern cities are **International Paper Co.**, to Memphis, Tenn., **Neenah Paper Inc.**, to Atlanta, and **Rayonier Corp.** to Jacksonville.

In addition to its headquarters move, MeadWestvaco said it is establishing a research-focused Packaging Innovation Center in Raleigh and consolidating its paperboard businesses into a packaging resources group. The group is comprised of paperboard mills located at Covington and Evadale, Texas; a pulp mill at Cottonton, Ala.; and paper mill at North Charleston, S.C. ■

Drought, Dry Conditions Gain In The South



Baseball Legend Satchel Paige once said: "don't look back, something might be gaining on you." That advice applies to the South this spring as drought and dry conditions advanced like giant pincers from the mid-Atlantic on the east and from the nation's mid-section on the west. As the U.S. Drought Monitor map shows, by late April drought or abnormally dry conditions prevailed across the entire region except for parts of northern Alabama and Mississippi, western Tennessee, coastal Georgia, and Northeast Florida. Timber prices already are being adversely affected. ■

USDA National Drought Mitigation Center
Released Thursday, April 20, 2006
Author: Rich Tinker, CPC/NCEP/NWS/NOAA
<http://drought.unl.edu/dm>

Bush, New Canadian Leader To Restart Lumber Import Talks

It's back to the bargaining table for the long, long-running dispute between the U.S. and Canada over softwood lumber imports from the north.

With political relations between the North American neighbors noticeably warmer since the Canadian voters elevated the Conservative Party to power in Ottawa, President Bush and Prime Minister Stephen Harper used the NAFTA summit meeting at Cancun to agree that they want the lumber negotiations restarted.

Mr. Bush, according to media reports, assured Harper that the U.S. is prepared to negotiate in "good faith" and in a "timely fashion" to resolve the issue. The prime minister said he was taking the president at "face value" that Washington wants a resolution to the stand-off, but added:

"I just reminded the president that Canada's position on this is very clear, and if we don't see a resolution, Canada is certainly going to pursue all of its legal options, as well as enhanced support for our industry, through this battle," he said.

Those statements from the top don't guarantee that new negotiations will succeed where others have failed. But at least the U.S. ambassador, David Wilkins, was emboldened to predict on Canadian television that a

solution could be reached by the end of the year.

But no one seems to have as yet convinced the Coalition for Fair Lumber Imports, which represents the U.S. lumber industry and its tree-grower allies, that a solution is at hand. It continues to blast away at the subsidies Canada bestows on its lumber manufacturers in the form of far below market price stumpage fees for public timber and the financial support from public funds provided that country's forest products industry.

Nor are U.S. manufacturers and tree growers ready to accept the repeated findings and rulings by NAFTA panels which deny Canadian lumber that enters this country is subsidized. Indeed, the Coalition has filed a lawsuit in U.S. federal courts to have the NAFTA actions ruled unconstitutional.

Maybe President Bush and Prime Minister Harper will find the magic formula for ending the lumber dispute. Certainly the climate for reaching a diplomatic solution has improved with the Canadian voters' removal of the U.S.-baiting Liberal Party from control of Canada's national government. But there's still the pesky problem of those subsidized trees that are the source of Canadian lumber coming into this country.

Meantime, the U.S. continues

to collect countervailing and anti-dumping duties totaling 10.8 percent on Canadian softwood lumber entering this country. The money is being held in a special fund that now amounts to about \$5 billion pending a settlement of the dispute. ■

Weyerhaeuser U.S. Mills SFI - Certified

All 68 Weyerhaeuser Company paper and wood mills in the U.S. have been certified as meeting the procurement provisions of the Sustainable Forestry Initiative (SFI) standard, the company announced.

In a news release, Weyerhaeuser said its manufacturing facilities have been independently audited and found to meet three key requirements for certification: knowing where their logs and chips come from and the type of supplier; monitoring suppliers' compliance with state Best Management Practices (BMPs); and promoting sustainable forest practices among log and chip suppliers.

All of Weyerhaeuser's U.S. forests previously have been independently certified as meeting the SFI standard. SFI is governed by an independent board with equal representation from environmental groups, the forest products industry, and the broader forestry community. ■

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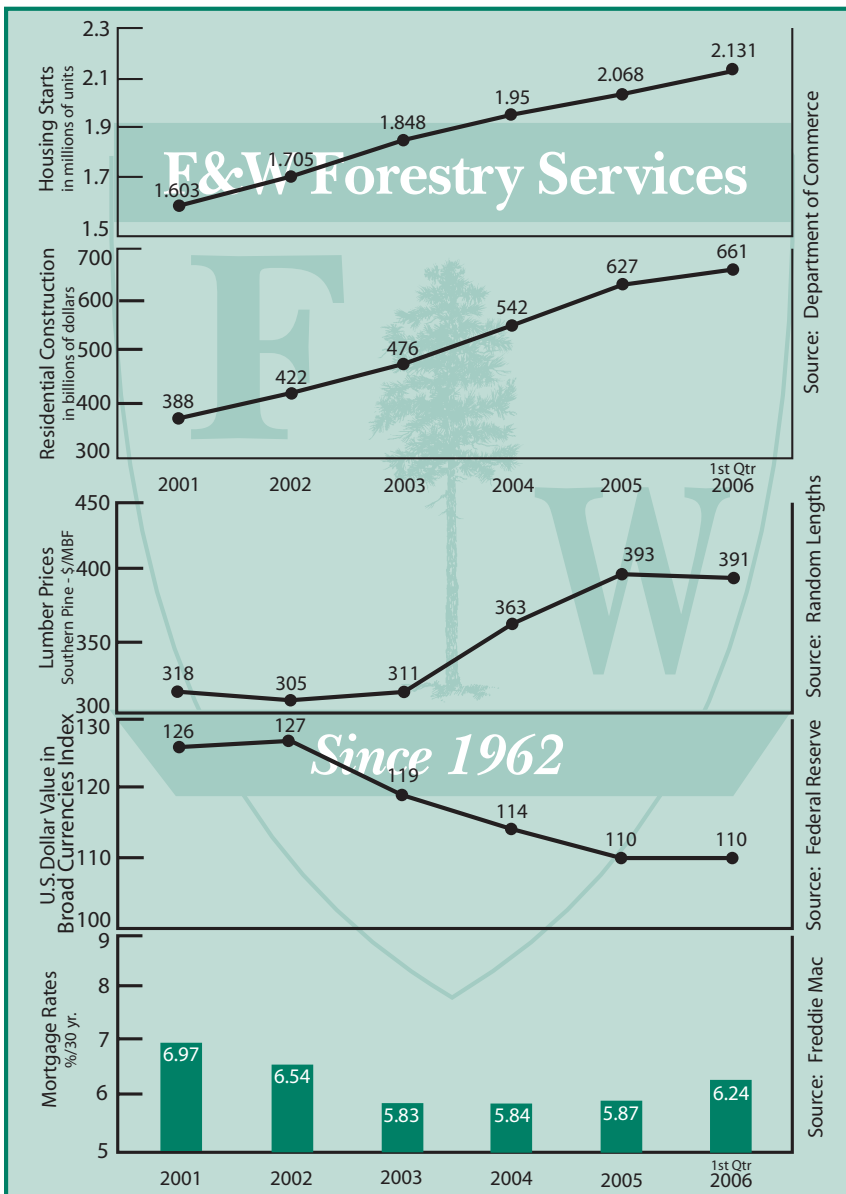
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Southern Timber Market Indicators



How Soft Is Soft?

A few months into 2006, the early indicators of the housing industry—whose fortunes are closely entwined with those of tree growers—are too mixed to get a clear reading for the year.

The numbers thus far show a decline in both housing starts and new home sales—not a good omen for prices and demand for lumber, OSB, and other wood construction materials that go into building those houses. Mortgage rates rose every month in the first quarter, continuing a trend that began last fall. The Federal Reserve, under a new chairman, continued to raise short-term rates, which is helping push up mortgage rates, although they remain low by historic standards.

On the plus side, housing starts for the first quarter, though down for each month, were at an annualized average rate of 2.131 million units—ahead of the rate of 2.068 million for all of 2005 as well as last year’s first quarter average of 2.083. The dollar value of residential construction continued to grow month-to-month, as it has since last June. And lumber prices, as measured by the Random Length Southern Pine Composite Index and by the cash and futures markets, remain stable and relatively strong.

So what’s with housing for the year? Slowing: definitely. Crashing: unlikely. Most knowledgeable housing experts have predicted a “soft landing” in 2006 all along. The question is: How soft is soft? ■