Knock on wood as the economy bites

FSF's portfolio of forestry has provided stability in volatile markets...

Update
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It is no secret that the last two years have been challenging for investors in almost all asset classes. Valuations have been dramatically re-rated across the board, a trend which is being reflected by investment trusts themselves, estimated to currently be sitting on their widest average discounts since 2008, according to Stifel.

In this context, it has become clear that even some of those assets investors consider the resilient staples within their portfolios can significantly falter in the face of particularly difficult macroeconomic conditions. Real assets for instance have suffered dramatic valuation downshifts, as rapidly rising interest rates impact the market for assets that are typically purchased with debt.

In this context, an asset class for which valuations have remained relatively stable is an intriguing prospect. Enter, UK forestry. The asset class may be a relatively newly investable one in a listed format, but its characteristics are unique. One aspect of this is that it benefits from the influence of not one but two separate markets in determining valuations.

Land that is able to be afforested is valued on the basis of both land prices and future timber prices. Unusually for a real asset, such land is typically not bought with debt, which has helped prices in this market hold up even as interest rates rise. Further, while demand for timber has fallen in the short term as increasing costs of living bite and the pace of construction and renovation projects slows, it is expected to rise significantly in the medium and long term due to embedded supply shortages which are impossible to rectify quickly because commercial trees take decades to reach harvesting maturity. While short-term shocks, such as storms, can increase the amount of timber coming to market, mature commercial timber can be harvested at any point over a five to ten year harvesting window, meaning that owners focused on total return as opposed to regular yield can delay harvesting should such a shock occur.

Forestry valuations are also supported by the broader business and policy context. With the need and demand for sustainability so high, forestry assets are in demand from a wide variety of buyers, seeking exposure for an equally broad number of reasons, both financial and sustainability-focused.

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London Stock Exchange listed **Foresight Sustainable Forestry (FSF)** takes this compelling investment proposition a step further. When acquiring assets, the team typically seeks to add 'natural capital alpha', i.e. generate additional value through their investing approach, which often comes as a result of improving the sustainability profile of these land assets.

While afforestation for the purposes of timber production is one example of the development value creation available with land assets, other alpha-adding opportunities include supporting carbon removal projects through planting and even aiding flood mitigation projects through land management.

The team also pursues a tactical acquisition strategy, which can include buying sites in close proximity to one another to introduce production synergies and economies of scale. As a trusted counterparty in the market, they often access properties that have not yet been listed publicly, giving the sellers a swift and reliable exit whilst also generating value for FSF.

The effectiveness of these techniques and the resilience of the FSF process have been demonstrated this week, when at its latest revaluation the trust's NAV appreciated by 3.5p per share to 108.5p, despite being determined amidst a subdued period for timber prices.

Although UK forestry managed sustainably in a listed format remains relatively under-served, global demand for forestry as an asset class is rising rapidly with increasing numbers of private funds being launched explicitly to target this opportunity. The Foresight team themselves have been investing in such assets for around five years already, with FSF launched a year and a half ago. Crucially, as the only trust investing in forestry and natural capital, it remains the only liquid route, in an otherwise relatively illiquid asset class, for most private investors to tap into this intriguing, diversifying and resilient part of the real estate sector.

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