

Deep roots and new branches

The universal drive for sustainability and the high inflationary backdrop has helped grow the investment case for timberland investing.

Sustainability and long-term return potential

Timberland investing provides investors with many of the same benefits as core real assets: a long-life physical asset with stable cash flows and protection against inflation. However, there are some key additional differences. A major benefit is that timberland allows investors to have a direct impact on climate change through carbon sequestration, as properly managed forests can help mitigate the harmful effects of carbon in the atmosphere.

Another key difference is the way timberland can generate income. Some forests produce trees that are harvested when mature, yielding logs that are cut in sawmills to produce lumber for construction. This process delivers returns that correlate strongly with housing demand, economic growth and ultimately inflation.

In fact, timberland offers the ability to respond opportunistically to changes in prevailing consumer prices. While the trees themselves increase in value slowly as they mature, the decision as to when and how much to harvest can reflect the prevailing prices for logs and wood.

We believe an active approach to forestry management can enhance returns ahead of the forestry index benchmarks over the long term (Exhibit 1).

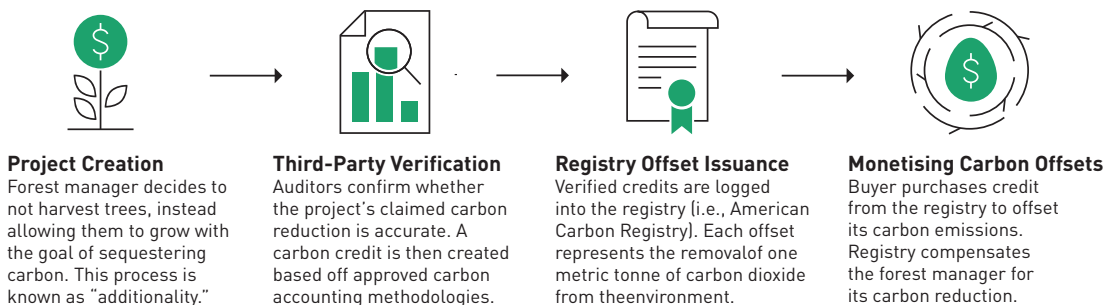
Reducing portfolio carbon emissions

As our economy moves in the direction of greater sustainability, the value proposition for timberland has evolved well beyond its use in construction. The value of a tree is no longer simply the harvest value of its wood, it also offers a powerful tool in the fight against global warming.

Forests are one of the most effective and scalable mechanisms for removing carbon from the atmosphere. They can serve as vast carbon sinks, with trees removing CO₂ from the atmosphere and using it as building blocks to increase growth and carbon storage. Sustainably harvested wood products and long-lived materials continue to store atmospheric CO₂ long after they have been removed from a forest. In addition to carbon sequestration, forests also provide other co-benefits such as clean water and wildlife habitat, recreational opportunities, and a source of living-wage jobs in rural communities.

The total annual level of global carbon emissions,

Exhibit 2: Carbon offset creation process



Source: J.P. Morgan Asset Management. For illustrative purposes only.

currently above 36,000 metric tons, will need to decline by approximately 10,000 metric tons to keep global temperatures within 1.5 degrees centigrade through the year 2100, in line with the Paris Agreement.¹ Limiting output is possible, but difficult. Direct offsets through carbon sequestration can meaningfully reduce the total while giving the global economy time to adjust to a more sustainable model.

While the carbon offset market is still young, the process by which carbon offset credits are created, verified, registered and sold is becoming increasingly institutionalised. Furthermore, there are a number of promising technologies focused on measuring, harvesting and locating buyers that could increase supply and broaden the market to include small and mid-size landholders. For the time being, however, the demand for offsets from corporations exceeds the supply leaving forestry owners in an advantageous position (Exhibit 2).

For timberland investors, the ability to generate income from trees while they grow is transformational: put simply, rather than waiting to get paid, they can now get paid to wait. Each layer of modern forestry management increases the value of timber. The unique benefit of carbon offset revenue, however, is that it does not require the tree to be felled in order to realise returns. Over time, this should keep more trees in the ground, benefitting the environment yet also reducing the overall timber supply (all else equal), and thereby supporting overall prices for cut wood.

Add diversification to portfolios

In volatile markets, the capacity of timberland to deliver steady returns with low volatility can improve portfolio efficiency while offering resiliency in the face of inflation and rising rates. According to research by J.P. Morgan Asset Management,² timberland can bring strong diversification properties to portfolios, with low correlation to major risk factors that dominate the performance of other asset classes.

In historical market stress events, this low exposure to major risk factors has helped forestry perform well compared to the majority of risk assets, with only modest losses (or even modest gains) produced through the biggest crises and rising rate scenarios of the last 20 years. This key attribute can help protect the value of portfolios during market downturns.

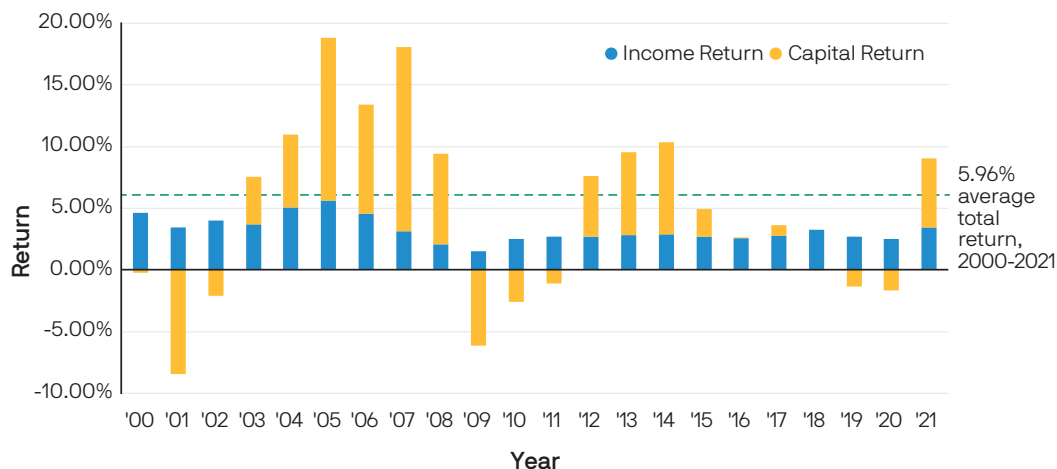
Investing with Campbell Global

In 2021, J.P. Morgan Asset Management acquired sustainable forest manager Campbell Global, which has a global portfolio of sustainably managed forests, providing the potential for investors to contribute to global emissions reduction efforts, offset their own portfolio emissions and to profit from carbon credits.

Campbell Global is a global investment manager with over 40 years of history managing active strategies focused on forestland. Based in Portland, Oregon, Campbell Global manages over \$5.5 billion in assets and its clients own around 1.7 million acres in forestry around the world.

Over the decades, Campbell Global has created value through its innovative thinking and dynamic approach to investing in and managing sustainable forests, deploying proprietary data and advanced modelling to attempt to derive maximum value from the properties it owns. (All data as of 31/12/2021).

Exhibit 1: Forestry performance broken out by income and capital return



Source: NCREIF US Timberland Property Index (year-end total return). Data as of December 31, 2021.

FOOTNOTES:

1 Source: Global Carbon Atlas (<http://www.globalcarbonatlas.org/en/CO2-emissions>); Carbon Registries (total of carbon offset registered on Climate Action Reserve, American Carbon Registry, Carbon Plan, Gold Standard, Verra, Clean Development Mechanism); ARB is not included since projects are also registered in American Carbon Registry, Climate Action Reserve, and Verra. Data as of 2019 – unless unavailable.
2 Source: J.P. Morgan Asset Management. Past performance is not indicative of future results. Based on factor loadings/estimates from returns data for the 18 year, 10 month period from January 2003 to November 2021. Analysis conducted on GBP hedged asset classes.

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