Demand for land use is bringing about a convergence of forestry and agriculture investment management. Florence Chong reports

RISE OF NATURAL CAPITAL

The paths of agriculture and forestry have started to intersect. The emerging question is just how two land-based sectors can best co-exist in a world of competing demands.

The two biggest institutional investment managers in both markets have set the trend over recent years. In 2021, Canadian insurance company Manulife merged its long-established real assets businesses into one arm, and last year, Nuveen (owned by TIAA), brought its €10bn agriculture and timberland portfolio under the one umbrella.

Meanwhile, New Forests has established a standalone agriculture business, New Agriculture, and its latest fund will combine forestry and agriculture.

There are many other examples, including New York-based Folium Capital Partners, which also once offered separate timberland and agriculture funds. Today, it has a commingled fund for both sectors. Central to these strategies is to give management visibility of how to best allocate land in the portfolio for optimal use in either forestry or agriculture.

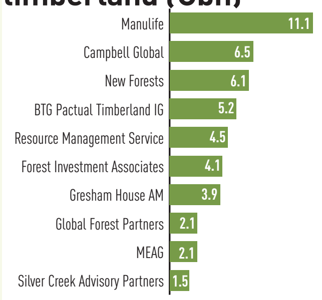
"This is exactly the approach we are trying to have," says Martin Davies, global head of Nuveen Natural Capital, which manages 3m acres across 10 countries. "We have brought our farmland and timberland platforms together to give us the opportunity to invest from the perspective of what is the best and most appropriate use of the

TOP 25 NATURAL CAPITAL MANAGERS

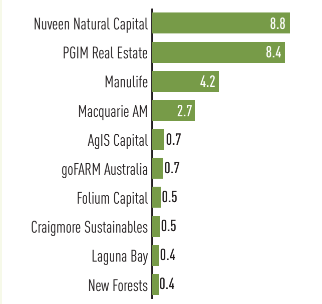
	Company	Natural capital AUM (€m)	Forestry/timberland AUM (€m)	Agriculture/farmland AUM (€m)	As at
1	Manulife	15,309	11,096	4,213	30/09/22
2	Nuveen Natural Capital	10,152	1,392	8,760	30/06/22
3	PGIM Real Estate	9,494	1,069	8,425	30/09/22
4	New Forests	6,530	6,126	404	30/06/22
5	Campbell Global	6,490	6,490	0	31/12/21
6	BTG Pactual Timberland Investment Group	5,184	5,184	0	09/11/22
7	Resource Management Service	4,521	4,521		30/09/22
8	Forest Investment Associates	4,099	4,099		30/06/22
9	Gresham House Asset Management	3,930	3,930		30/09/22
10	Macquarie Asset Management	2,703	0	2,703	31/12/22
11	AXA IM Alts	2,405	875	0	01/09/22
12	Global Forest Partners	2,133	2,133		31/12/21
13	MEAG	2,130	2,130		31/12/22
14	Silver Creek Advisory Partners	1,509	1,509		30/06/22
15	Folium Capital	968	410	558	31/12/22
16	AgIS Capital	753		753	07/11/22
17	goFARM Australia	695		695	14/12/22
18	Craigmore Sustainables	655	158	497	30/09/22
19	Mirova	566			30/09/22
20	Laguna Bay	442		442	23/12/22
21	SLM Partners	408	33	375	31/12/22
22	Lazard Asset Management	277	24	253	30/09/22
23	Amundi Real Assets	265	166	99	31/12/21
24	Jamestown	262	262		30/09/22
25	Aquila Capital	192	106	87	30/06/22

Source: IPE Research

Top 10 forestry/timberland (€bn)



Top 10 agriculture/farmland (€bn)



land in question."

Davies says that assessment of land use is ongoing. "In some situations land could be in agriculture production, but it becomes more important that it is sustainable agriculture production when you are looking to reduce the carbon footprint," he says.

"You could switch to forestry if that land is marginal in agriculture and you are not getting appropriate output from the input you are investing. In such an instance, it may be appropriate to revert the land to climate vegetation."

If the best use is not agriculture, timberland or climate vegetation, there could be other options, such as the installation of solar panels. It is a question of looking for best use of land, says Davies.

He has no doubt that the integrated, holistic approach will become more common to the management of land-based investment. Davies adds that it will be necessary to improve commercial production and to reduce the carbon footprint, alongside a strategy of protecting existing habitat – or restoring habitat where commercial production does not make sense.

"There is now conflict in land use, but that is why we can't think of forestry or agriculture individually any longer," he says. "We need to have an integrated approach."

Eric Cooperstrom, managing director, impact investing and nature capital solutions, at Manulife Investment Management, says Manulife is looking to optimise land use and sustainability across its timber and agriculture businesses.

"From the farmland side, we tend to make acquisitions of highly-productive agricultural land," he says. "Moving a significant portion of that into an alternative use like timberland often does not make economic sense."

Cooperstrom says the conversion of lower-quality and degraded pastureland into timber plantations is a viable strategy. "Carbon is going to be increasingly important part of our business, but at the same time there are some long-term tailwinds for traditional sustainable timber management."

Generally, there is a finite supply of timberland, he adds. Reforestation and afforestation notwithstanding, there are only so many productive timber assets located near integrated mill processing infrastructure.

"There is going to be continued demand for high-quality, timber-producing timberland and a desire by investment managers and others like ourselves to sustainably manage these assets and to provide sustainable fibre to the market."

The United Nations Principles of Responsible Investment (PRI) predicts that nature-based solutions to the climate crisis focused on reforestation and afforestation could generate US$800bn in annual revenue by 2050, with assets valued at well over US$1.2trn. This would surpass the current market capitalisation of the oil and gas majors.

Sydney-headquartered New Forests has started a pilot project known as ActivAcre in Tasmania, Australia's southern-most state.

David Brand, New Forests' chief executive, says technology has made it possible to isolate land areas that are currently not productive.

"We look at a farm and we might say to a farmer that 30% of the land is not commercially attractive for grazing or cropping," Brand says. "We will lease the land to grow trees. The farmer gets a fixed income and the marginal land is used for forestry."

So far, says Brand, around 50 farmers are looking to partner in the ActivAcre project. The concept is being incorporated into a new landscape fund that was launched in December. This fourth-generation New Forests vehicle, the A$600m (€385m) Australia New Zealand Landscapes and Forestry Fund, will offer flexibility to invest across land uses.

New Forests, which manages more than 1m hectares of investments valued at A$10bn, intends to manage agriculture and forestry as combined assets in this fund.

"We use a much more granular approach to extract value. This allows us to do more novel investments because the days of just buying extensive forestry estates are over," says Brand.

"Large forests have already been sold into institutional investor ownership and now we need to find more interesting approaches to get money to work and to create good returns for investors.

"This is just one of the big trends in forestry made possible by a huge expansion in the use of analytic tools, particularly geospatial analysis and mapping."

Brand, who established New Forests in Sydney in 2005, says: "Until now, you didn't have transparency with underutilised land. In the US, we have created a geospatial modelling approach using heat maps to tap into unrealised climate mitigation value. We buy this for the net present value of the forestry cashflow. In doing so, we have been able to add 200-400bps of excess returns, a strategy that gives us a competitive advantage."

Forestry has evolved to be a multi-market natural capital investment, Brand says. Tools are now available to help managers better extract more value from landscape optimisation. "We can now allocate land for conservation, for food production or for forestry. This enables us to continuously extract higher returns for our investment capital."

Folium Capital manages US$900m in forestry and agricultural assets. When it launched its first funds in 2016, there were separate vehicles for each, says Andy Wiltshire, Folium Capital co-founder and managing partner. Folium has since changed its approach.

"We are merging our agriculture with our forestry investment streams," says Wiltshire. "Some properties have potential to grow trees in one area and agriculture in another. Where water rights are available, it may be best to grow high-value produce on that land.

"You can put almond or avocado orchards into these areas. But land at the back of the same property which does not have the same good soil may be best used to grow trees for a combination of timber and wood products and carbon."

Folium has a strong focus on carbon forestry, developing new forests on degraded farmland. The Folium partners were early adopters of a voluntary carbon-credit scheme in Uruguay back in 2007.

"As carbon markets have developed, we have become more focused on the carbon component of forestry, because the economics are shifting towards this compared to the timber component," says Wiltshire.

According to the World Resources Institute, around US$350bn in new investment for agriculture will be needed each year to meet growing global demand for food. Land is also needed to produce timber and fibre for materials substitution to reduce carbon emissions, if net-zero targets are to be met by 2050.

Byfield plantation forest in Queensland, Australia (source: CNW Group/Manulife Financial Corporation)

Global Timber Outlook 2020, a paper by Gresham House, says timber consumption will rise from 2.2bn cubic metres in 2020 to 5.8bn in 2050. Gresham House has £3.29bn (€3.72bn) in timberland assets under management in the UK, Australia and New Zealand.

It says the forecast rise in timber demand is set against constrained supply fixed by the long-term growth rate of trees and limited land areas. The current forecast for long-term sustainable timber supply between now and 2050 ranges from 3.7bn cubic metres to 4.7bn.

Questions remain for the forestry sector. Should they be restricted to carbon sequestration or also used for timber products? Should owners rotate the planting of tree species (conifers and pines mature in 30 years, while broad-leaved species like oak can take up to 80 years to mature)?

Timberland managers are also at odds over whether single-specie plantations should be discouraged because such estates lack resilience. For example, in places such as Scotland they have been shown to suffer more damage than mixed-variety forests during severe storms.

The industry recognises that there are emerging issues and these have to be managed. For now, there is no consensus at an industry or regional level, let alone a global approach to forestall emerging issues from becoming major problems.

The debate is playing out against a background of self-interest. The scientific community is focused on a nature-based solution to deal with climate change. Other groups have their own priorities.

Davies says: "Globally, people are not thinking through some of these issues, or the consequences of the impact of government policy in individual locations. It will be something that comes into focus when there is a realisation of the repercussions of some of the questions now being raised."