

2006 Timberland Investment Performance

Despite the downturn in demand for housing and associated manufactured wood products, U.S. timberland properties in the NCREIF Timberland Index returned 13.7 percent for calendar year 2006.

As in prior years, we devote our fourth quarter issue of the *Hancock Timberland Investor* to a review of investment performance of U.S. private timberland properties.

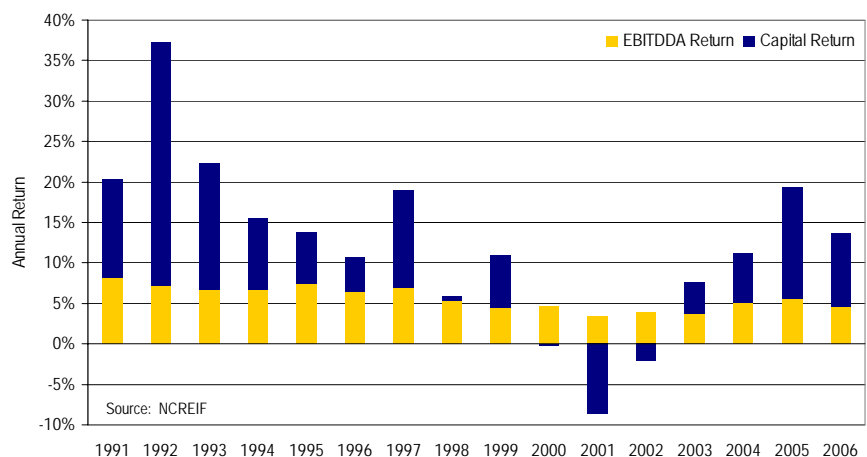
Our measure of timberland performance is the NCREIF (National Council of Real Estate Investment Fiduciaries) Timberland Property Index (See *HTI 3Q 2000 for a description of the Index*), which reports returns for institutional investments in timberland properties throughout the United States.

NCREIF timberland properties numbered 261 as of fourth quarter 2006, 26 more properties than at year-end 2005. These properties contained over 5.9 million acres of timberland in the United States, with a combined market value of \$9.2 billion. Sixty-one percent of the Index value was in the South, 29 percent in the Pacific Northwest and the remaining 10 percent in the Northeast.

Performance Results

U.S. timberland properties continued to generate strong returns during 2006. The total return reported by NCREIF was 13.7 percent. Cash yields fell from 2005 levels, but remained above 4.0 percent. As a comparison, S&P 500 stocks returned 16 percent, long-term bonds

Chart 1: NCREIF Timberland Property Index - Annual Returns



3.5 percent and commercial properties 17 percent.

Timberland returns are comprised of two components, property-level income from operations or EBITDDA, and capital appreciation or depreciation, reflecting the change in asset values. The EBITDDA return was 4.6 percent – a value similar to the average over the past ten years. The cash yield from operations after deductions for capital expenditures was 4.1 percent.

NCREIF capital returns were a positive 8.8 percent – a drop of over

400 basis points from the double-digit capital appreciation in 2005.

Chart 2: 2006 NCREIF Regional Timberland Returns

	Pacific		
	South	Northwest	Northeast
EBITDDA	3.4%	7.2%	2.9%
bps change from 2005	11	-274	-688
Capital	11.4%	6.7%	-2.0%
bps change from 2005	69	-1710	-348
Total	15.1%	14.3%	0.88%
bps change from 2005	83	-2137	-1014

(Continued on page 2)

Regionally, timberland in the Southern U.S. produced the highest returns over the year at 15.1 percent. Properties in the Pacific Northwest returned 14.3 percent. Income returns were down considerably from last year in the Pacific Northwest - at 7.2 percent. Properties in this region typically contain a greater share of mature, merchantable timber that is available for harvest, resulting in a higher income return as compared to other regions in the U.S.

Properties in the South are typically comprised of younger-age timber, and therefore have lower income returns. This year's EBITDDA return in the South, at 3.4 percent, is not unlike prior years.

What drove Timberland Performance?

NCREIF timberland market values in 2006, as measured by appraisals and actual timberland sales, rose in both the South and the Pacific Northwest. To isolate the influence of changing timberland market conditions from the effect of timber inventory growth and changes in the sample of properties in the Index, we recalculate timberland values to represent a standardized 'fully-regulated' forest based on NCREIF total returns (See HTI 2Q 2002 for a full description of our methodology).

Movements in market value can generally be explained by movements in timber prices and changes in discount rates.

Historically, real timber prices and property values in the U.S. peaked during the mid to late 1990s, and then declined substantially during 2000, 2001, and 2002 in response to falling levels of operating cash flows. Real timberland property values rose on average by about 20 percent during 2005 and 2006.

Chart 3: Operating Cash and Market Value for U.S. South All Age Forest

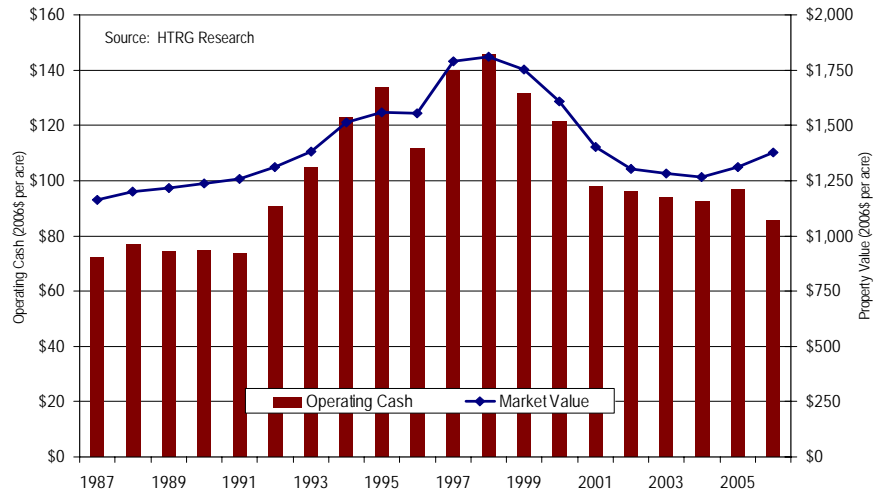
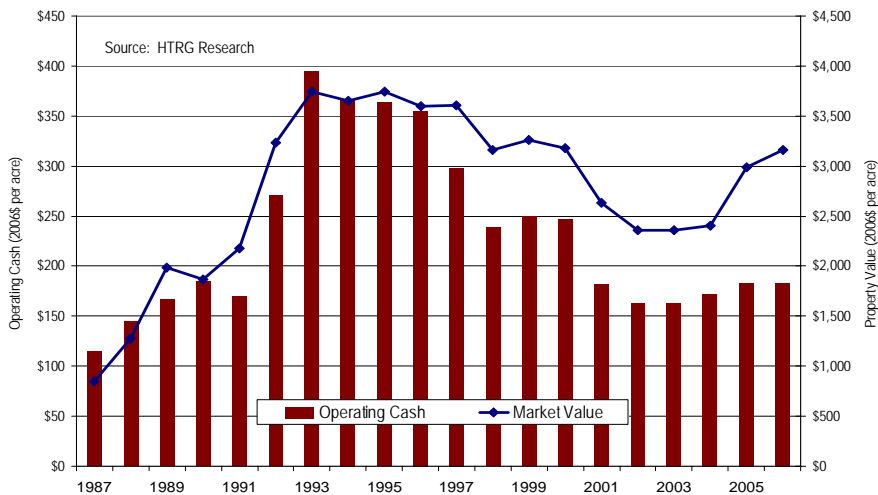


Chart 4: Operating Cash and Market Value for U.S. Pacific Northwest All Age Forest



Our inflation-adjusted market value estimates for 2006 rose 5.1 percent in the South and 5.5 percent in the Pacific Northwest over values last year. Despite the increase, current values remain nearly 20 percent below peak levels in real terms.

Rising market values should potentially be attributed to increases in timber prices and/or falling discount rates.

Examining timber prices in Figures 1 and 4 (on pages 3 and 4) reveal downward movement in nearly all domestic stumpage prices in the fourth quarter.

At the same time, cash yields or real discount rates for timberland, calculated as a ratio of net operating income to land value, have declined in both the South and the Pacific Northwest. Southern timberland cash

(Continued on page 6)

Quarterly Average Regional Composite Prices for Softwood Sawtimber Stumpage (U.S.\$ per MBF)

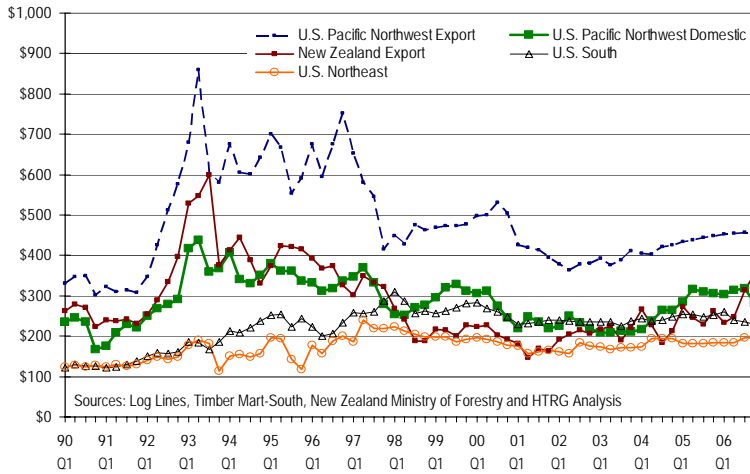


Figure 1. Softwood Sawtimber Stumpage Prices

Prices for New Zealand export logs, in US\$ terms, continued upward fourth quarter, rising another 13 percent on top of last quarters gains for a total increase of 35 percent over export prices a year ago. Log demand in Asian markets remains strong, and log supply tight, particularly in Korea, pushing price levels up. Stumpage prices for domestic softwood in both the US Pacific Northwest and the US South finally felt the effects of this year's fall in prices for lumber and wood panels. In the U.S. South, pine sawtimber stumpage prices dropped 3 percent from last quarter to average \$229 per MBF. Domestic sawlog stumpage in the U.S. Pacific Northwest fell almost 10 percent from last quarter levels, averaging \$282 per MBF for the fourth quarter.

Quarterly Average Prices for U.S. South Lumber and Sawlogs (\$ per MBF—lumber scale)

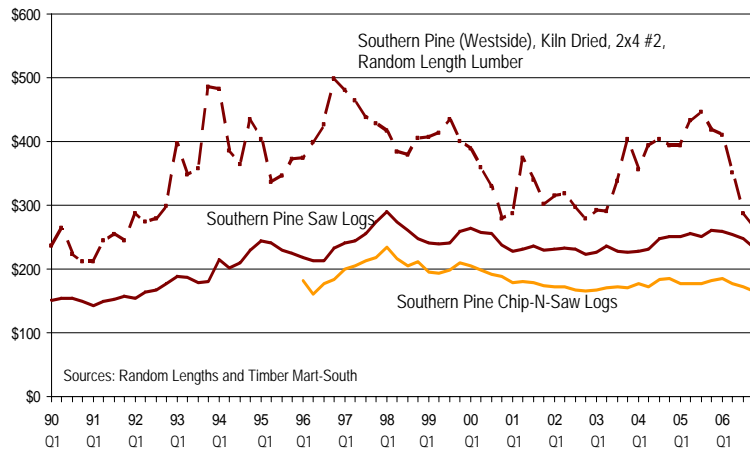


Figure 2. Lumber and Sawlog Prices in the U.S. South

Southern pine lumber prices dropped 6 percent on average from last quarter despite a short-lived December increase, ending the fourth quarter at an average price of \$268 per MBF. Prices for kiln-dried southern pine 2x4's were down 35 percent from year-ago levels of \$418 per MBF. Delivered log prices for both sawtimber and chip-n-saw have finally moved lower as expected, lagging the fall in prices for lumber and wood panels. Delivered log prices dropped 5 percent on average from last quarter, and declined 10 percent from fourth quarter levels a year ago.

Quarterly Average Prices for U.S. Pacific Northwest Lumber and Sawlogs (\$ per MBF - lumber scale)

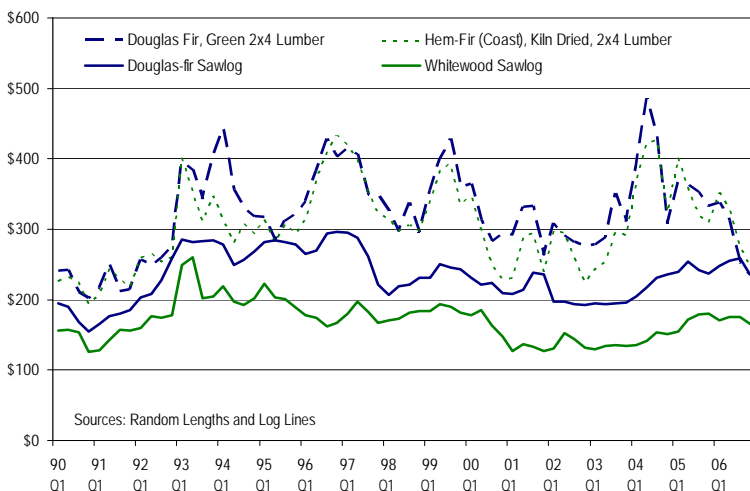


Figure 3. Lumber and Sawlog Prices in the U.S. Pacific Northwest

The continued decline in housing demand weighed heavily on lumber and wood panel producers – estimates of lumber consumption for 2006 look to be 4 percent off of 2005 levels, and further declines in demand are expected for 2007. In the U.S. Pacific Northwest, lumber prices fell 8 percent on average from prices last quarter. Hemlock lumber prices took the heaviest discounts. Kiln dried hemlock 2x4's fell 11 percent from last quarter, averaging \$246 per MBF. Douglas-fir green 2x4 prices dropped 7 percent from last quarter to average \$236 per MBF. Delivered log prices in the Pacific Northwest moved lower, after holding steady for most of the year in the face of falling lumber and wood panel prices.

**Quarterly Average Regional Composite Prices
Softwood Pulpwood Stumpage (\$ per ton)**

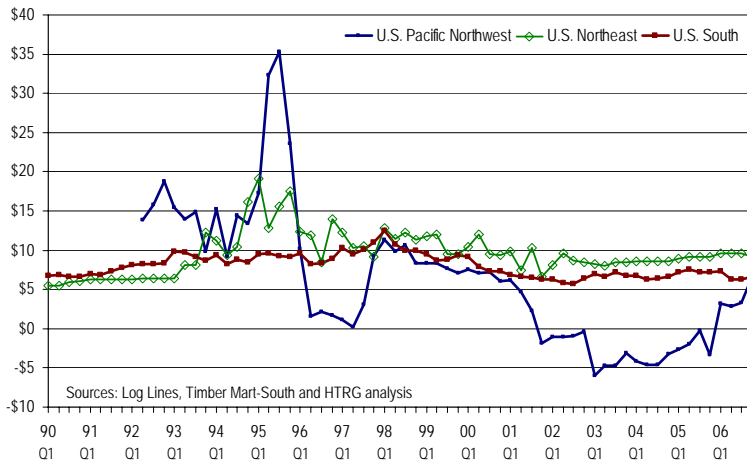


Figure 4. Softwood Pulpwood Stumpage Prices

Pulpwood prices were flat-to-up in all regions of the U.S. fourth quarter. Prices for pulp logs in the Pacific Northwest showed the greatest percentage change in increase over last quarter as demand continues to outpace the supply of pulp logs in the region. As lumber production slows, less sawmill residual chips have been available for pulp mills, increasing the demand for whole logs. In the South, pulpwood prices average \$6.60 per ton, up \$0.30 per ton from last quarter, yet down 8 percent or \$0.55 per ton from fourth quarter last year.

**Quarterly Average Prices for Market Pulp
(\$ per metric ton) and U.S. Pulp Logs (\$ per 10 tons)**

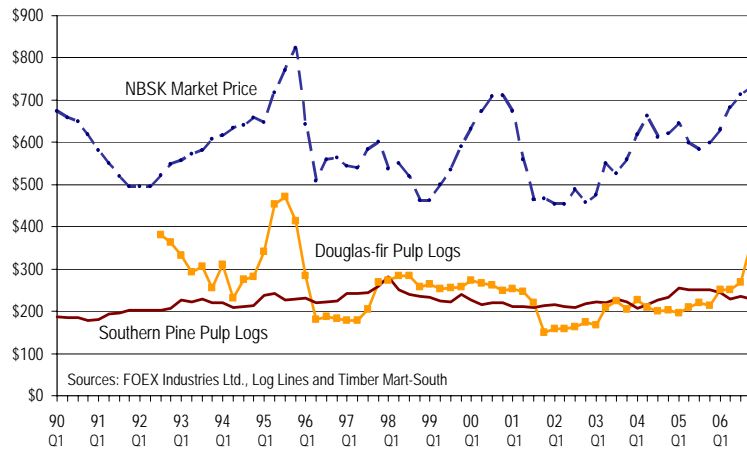


Figure 5. Market Pulp and U.S. Pulp Log Prices

The price for NBSK market pulp rose to \$730 per metric ton fourth quarter, a level not seen since mid-1995. Douglas-fir delivered pulp logs rose this quarter as well, and likewise, ended the fourth quarter at levels not reached since 1995.

Quarterly U.S. Timberland Values (\$ per acre)

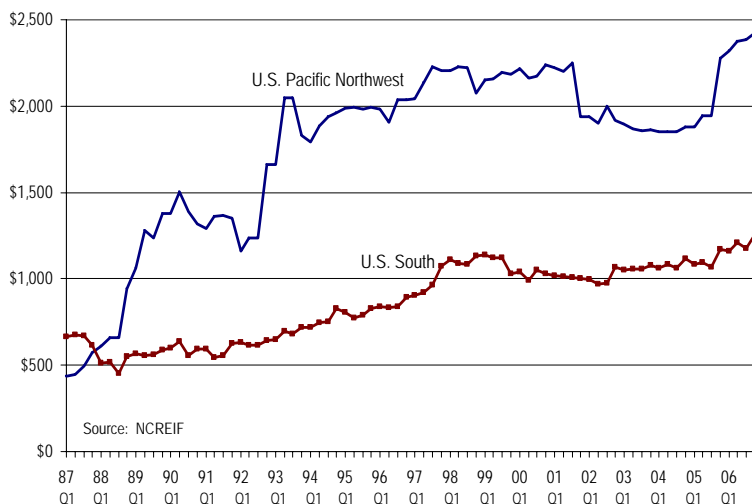


Figure 6. U.S. Timberland Values in Private Property Markets

The value of private U.S. timberland at year-end 2006, as measured by the properties in the NCREIF Timberland Index, increased 10 percent over values at year-end 2005. Timberland properties in the South appreciated 7.4 percent over prices last year, ending the year at \$1,260 per acre. Timberland properties in the Pacific Northwest rose 6.5 percent over last year, averaging \$2,425 per acre at year-end.

**Quarterly EBITDDA Multiples for Privately Traded
Timberland (trailing 4-quarter EBITDDA)**

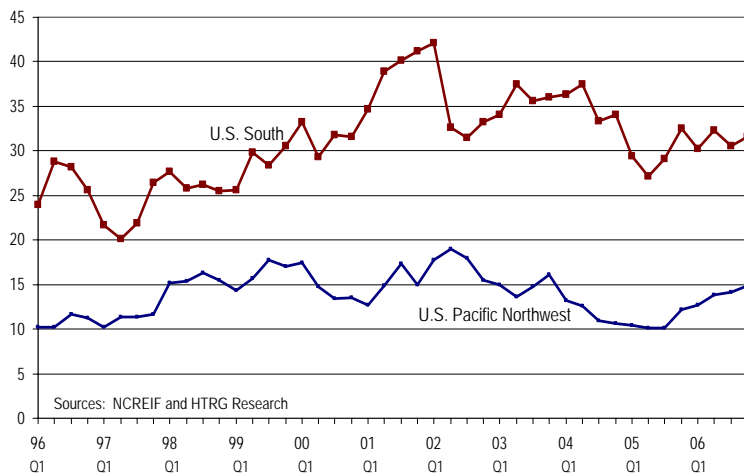


Figure 7. U.S. Timberland Valuation Multiples in Private Property Markets

Steady earnings and rising timberland market values boosted southern price-to-earnings multiples upward fourth quarter. Multiples were held up by a greater degree in the Pacific Northwest, as rising timberland market values combined with falling income, dropping on average about \$6 per acre from fourth quarter of last year.

**Monthly Securitized Timberland Share Value
(Indexed to 100 at start date)**

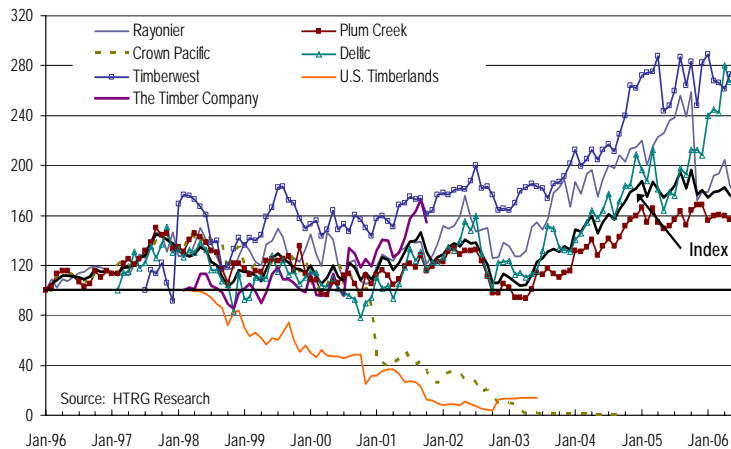


Figure 8. Hancock Securitized Timberland Index

Our measure of timber-intensive public company value – the Hancock Securitized Timberland Index – ended the quarter 14 percent above third quarter’s ending value. Despite declines in lumber and panel markets, earnings remained strong due to the strength in export log markets, only moderate declines in domestic log prices, and executing real estate sales where available.

Quarterly U.S. South Timberland Values (\$ per acre)

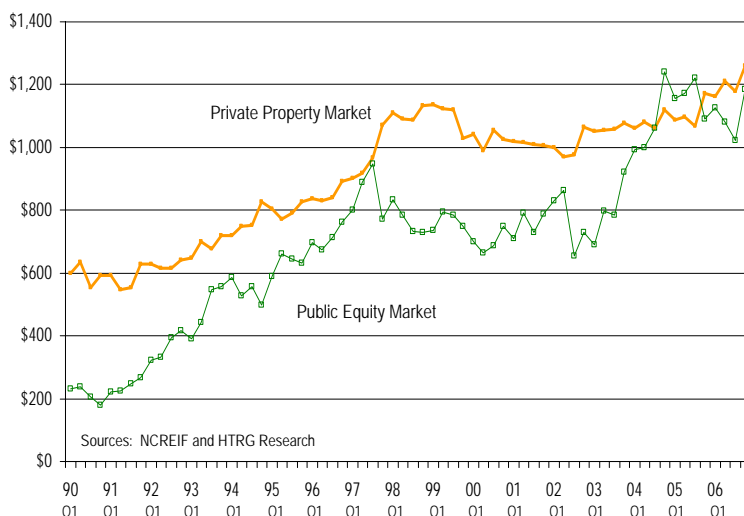


Figure 9. U.S. South Timberland Values in Public Equity and Private Property Markets

Market values for timberland in the South increased in both private and public markets. The difference in value between the two markets remained similar to year-ago levels, with private timberland valued about \$75 per acre greater than public market timberland.

yields fell 115 basis points. In the Pacific Northwest, 2006 yields were down 30 basis points from last year, for a total decline over the past two years of 135 basis points.

The increases in timberland values therefore, would seem to be attributable to decreases in the discount rate rather than any increase in timber prices.

Comparative Yields

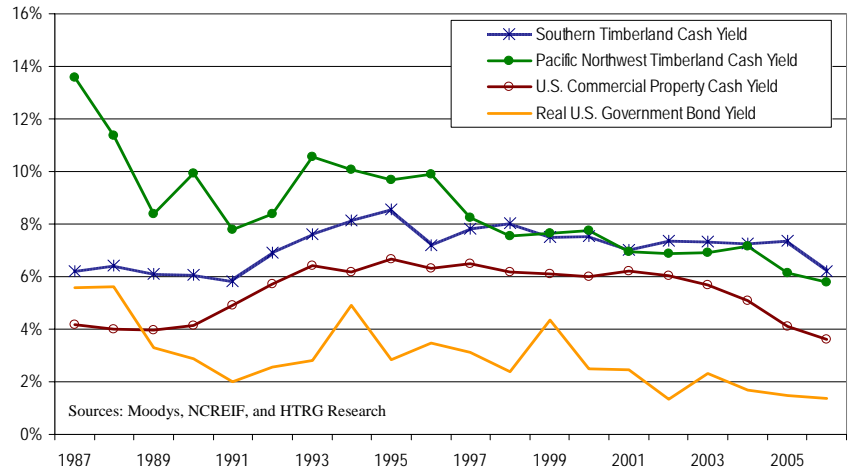
Over the past decade, operating cash yields in both the South and the Pacific Northwest have trended downward, but have fallen by lesser amounts than other assets. Commercial real estate yields in the U.S. have fallen recently by 300 basis points.

The current spread between commercial properties and U.S. government bonds is 200 basis points, down from 500 basis points five years ago.

premiums relative to commercial real estate properties and government bonds. There appears to be room for further modest declines in U.S. timberland yields.

Timberland properties are currently priced to return historically high

Chart 5: Cash Yields for U.S. Timberland Properties



NOTES:

Figure 1. The composite price for southern sawtimber is based on quarterly average Timber Mart-South published prices for pine sawtimber and chip-n-saw stumpage. Pacific Northwest prices are derived from quarterly average Log Lines published prices for whitewoods and Douglas-fir with internal analysis of logging costs for stumpage calculations. New Zealand export prices are based on New Zealand Ministry of Forestry quarterly average published prices for radiata unpruned A, J, and K sort export logs with internal analysis of logging costs for stumpage calculations. Northeast sawtimber prices are calculated from internal analysis.

Figure 2. Quarterly southern pine (Westside), kiln dried, 2x4 #2 lumber price published by Random Lengths. Timber Mart-South published southern pine sawlog and chip-n-saw log prices converted to lumber scale using RISI historical lumber recovery rates as published in their North American Lumber Forecast.

Figure 3. Quarterly Douglas-fir, green 2x4 lumber (Portland rate) and Hem-Fir (coast), kiln dried, 2x4 lumber prices published by Random Lengths. Douglas-fir and whitewood sawlog prices derived from Log Lines published priced for #2 and #3 sawlogs in various regions in the Pacific Northwest converted to lumber scale using RISI historical lumber recovery rates as published in their North American Lumber Forecast.

Figure 4. Pulpwood composite prices are derived from quarterly average Timber Mart-South published prices for southern pine pulpwood stumpage, Log Lines published whitewood and Douglas-fir pulp logs with internal analysis of logging costs for the Pacific Northwest, and HTRG analysis of spruce/fir pulpwood in the Northeast.

Figure 5. Quarterly NBSK pulp priced derived from daily list prices

reported by FOEX industries Ltd. Southern pine pulp log prices published by Timber Mart-South. Pacific Northwest Douglas-fir pulp log prices published by Log Lines. Pulp log prices expressed in multiples of 10 to accommodate market pulp pricing scale.

Figure 6. Regional NCREIF timberland market value per acre is derived by dividing the total regional market value at quarter end by the number of acres reported in that region.

Figure 7. EBITDDA multiples are calculated using NCREIF timberland value per acre at quarter end divided by trailing four-quarter average NCREIF net income per acre.

Figure 8. The Hancock Securitized Timberland Index (HSTI) uses a base-weighted aggregate methodology (similar to that used to construct the S&P 500) to calculate a market capitalization-weighted value for seven publicly traded timber-intensive forest products companies. Base weights were adjusted for the emergence of new companies or at the beginning of each year. Dividends are not reinvested. The companies included in the HSTI have no investment relationship with Hancock Timber Resource Group.

Figure 9. Public equity values are derived from our Timberland Enterprise Value per Southern Equivalent Acre (TEV/SEA) calculation for five timber-intensive publicly traded companies as compared to southern timberland values per acre calculated from the NCREIF database. TEV is a quarterly estimate based on total enterprise value (total market equity + book value debt) less estimated value of processing facilities, other non-timber assets and non-enterprise working capital. SEA uses regional NCREIF \$/acre values to translate a company's timberland holdings in various regions to the area of southern timberland that would have an equivalent market value.

References to expected investment performance in this newsletter are based on historical information and are based on managements projections. Potential for profit as well as for loss exists.

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