

Jim Hourdequin, Managing Director, The Lyme Timber Co., Hanover, NH

Note: As timberland Investment Management Organizations (TIMOs) go, The Lyme Timber Co., based in Hanover, NH, is one of the nation's oldest and most distinct. Lyme's Managing Director, Jim Hourdequin, 38, who has a background in logging, touches on the TIMO's history, style, operating philosophy, relationships with loggers and consuming mills and more. He also offers his opinion on the logging capacity issue, the importance of loggers to the organization, the challenges of operating a logging business, and the logger-related positive/negative impacts that have evolved with the ongoing structural shift in timberland ownership in the U.S.



Jim Hourdequin

Give a brief history of The Lyme Timber Co.

Lyme was formed in 1976 as a partnership to invest in timberland. Early holdings included lands in Virginia, West Virginia, Pennsylvania, Wisconsin, New York, and New Hampshire. This was before the term "TIMO" even existed and timberland was a fairly illiquid asset. In the 1990s Lyme began focusing on conservation opportunities, selling lands in fee to public agencies, selling conservation easements, and doing limited development projects.

The company also began investing in commercial real estate in the Boston area, eventually establishing a \$1.5 billion portfolio that dwarfed the timberland business. I joined Lyme in 2005 just as the commercial real estate business was being sold. The founding partners retired, we restructured the company, and returned our focus to timberland with an emphasis on conservation transactions and sustainable forest management.

What, if anything, sets the entity apart from other TIMOs?

I would say three things, the first being that we are value investors; we don't buy properties on the basis of appraisals or what others are doing in the market. Instead we analyze each property from the bottom up based on its potential for timber income, biologi-

cal growth, conservation sales, and other sources of value. We've sat out markets that appear overheated and our portfolio has grown much more slowly than some other TIMOs despite our being one of the oldest.

Second, we like to recover a portion of our investment through the sale of a working forest conservation easement, or WFCE. We've sold WFCEs on 600,000+ acres of timberland over the past 10 years. The easements restrict development but allow for ongoing timber harvesting and management. We like easements, as well as long-term timber deeds, because they concentrate our investment on the timber resource rather than some of the more speculative aspects of owning timberland—conversion to other uses and breakup value.

A third thing that sets us apart is our focus on forest operations. We own and operate log concentration yards—currently in New York, Tennessee and Wisconsin—and contract directly with loggers and truckers for cut-and-haul services. We try to establish long-term relationships with contractors and mills and we produce a steady volume of wood each year.

How many acres does Lyme now manage and how does it rank among other TIMOs in this respect?

At present we own approximately 400,000 acres, down from over 650,000 acres in 2007. Of the 15 or so TIMOs that are most active, we are probably number 11 or 12 in terms of size. However, that can change quickly as we are always looking to buy new properties. Right now we have approximately \$200 million of capital available for new acquisitions.

Where is this property located?

Our major timberland properties are in New York (246,000 acres), Tennessee (80,000 acres), Maine (20,000 acres), and Wisconsin (72,000 acres). We expect to acquire an additional 50,000 acres in the Southeast later this year.

Will Lyme continue to expand into other regions or perhaps invest in timberland located in other countries?

We would like to expand in the U.S. and Canada, but for the time being we have no plans to look beyond these countries. As we evaluate new regions of the U.S. we tend to focus on larger properties where we can fully deploy our operating strategies.

How much of the organization's managed property consists of actual working forests?

Right now almost 100% of the land in our timberland portfolio is working forest. At times our conservation holdings will include set-asides in ecologically sensitive areas, but in general these areas do not account for a large percentage of the land base. We also invest in wetland and stream mitigation banks, and some of these properties are not working forests.

How much fiber volume is typically harvested from these lands each year?

Last year we harvested about 700,000 tons—about 60% pulpwood, the remainder sawtimber. We expect to harvest about the same volume this year.

How many independent contractors does the organization work with and what types of harvesting methods are used?

In a given year, we work on a regular basis with between 50 and 60 different logging and trucking contractors on a regular basis. There are a number of different harvesting methods used depending on the site and the contractor. Feller-buncher and grapple skidder systems dominate our New York property. Hand felling combined with grapple skidders is most common in Tennessee. In Wisconsin there are a number of fully mechanized cut-to-length crews. We like to have a diversity of systems because no one system is right for all conditions.

Elaborate on your logging background.

When I was an undergraduate at Dartmouth College I got to know a local logger named Russell Barnes who periodically came to campus talks on environmental issues. I majored in biology and did research in forest ecology, but did not have a job after graduation. Russell was trying to start a safety group for contractors to lower the cost of workers' compensation, and he recruited me to help. We formed an organization, engaged an insurance company to provide coverage, and got OSHA funding to provide safety training. The organiza-

tion had moderate success initially, but even with lower insurance rates, there were simply too few contractors with bona fide employees to make a safety group viable.

Through the safety and insurance work, I became fascinated with the forest products industry and the challenge of building a profitable logging business that could provide good wages and benefits to skilled employees. So, somewhat naively—given no real business or logging experience—I and a good friend went into business with Russell and formed Long View Forest Contracting. We raised \$90,000 of capital from friends and family and used these funds and additional financing to buy a new Rottne forwarder to supplement an old forwarder that Russell owned.

What was your role in the logging business?

During the early years I spent a lot of time in the office, building systems for tracking costs and job profitability, figuring out employee compensation, and bookkeeping, while also managing the safety organization. Once the safety organization wound down, I was able to split my time between the office and the woods, where I worked as a chopper, felling trees for one of the two crews. Although I didn't set any production records, working in the woods proved invaluable to my career—specifically the time I spent looking at logs and trees, making bucking decisions, and understanding all the variables that go into a successful logging job.

You went from logging to the Harvard Business School?

After five years in business, we were in a position to hire an office manager, and I decided it was a good time to get some formal training in business and finance. I attended the Harvard Business School where I was the only student with a background in the forest products industry. I spent many weekends back at the business over the two years, and then spent the summer after graduating catching up on things that needed attention. I considered returning to the business full time, but despite its continued growth, the business did not need a full time person in finance. So I was very fortunate to land a position at The Lyme Timber Co., which is only about 45 minutes from where Long View is based.

What is your current role at Long View?

A few years ago, Russell Barnes, Jack Bell and I bought back the stock from the outside investors and now we each own a third of the company. We have an excellent team of people and Jack provides steady leadership. My role is limited. I continue to be involved in investment decisions, analysis, and business systems, but Jack and our office manager, Laurie Comstock, manage the day-to-day operations. Long View has grown to four cut-to-length crews, three of which are fully mechanized, and employs about 14.

The company recently added a forest management division that will create some new opportunities for growth. Some of the long-term employees plan to buy into the ownership structure and the business continues to work toward the original goal of providing good wages and benefits in a very challenging industry.

Describe Lyme Timber's relationship with logging contractors and elaborate on their importance to its long-term goals and operating philosophy.

Because Lyme owns lands that are subject to working forest conservation easements (WFCEs), we regard timber operations as the main driver of long-term value. The WFCE usually restricts our ability to develop the property or make financial returns from breaking it up into smaller pieces. What we have is a yield-producing asset, and our job is to manage it for income and timber appreciation. Having good, long-term relationships with quality logging contractors is critical to this strategy. We try to maintain relatively even harvest levels from year to year to sustain these relationships, as well as relationships with mill customers.

The foresters who manage our lands are very good at making sure logging jobs are fully set up before crews arrive, maintaining an inventory of wet weather work in the event a crew needs to move, and helping the logging contractor troubleshoot any challenges on the job, such as stream crossings or road building needs. We think supervision is expensive and we look for contractors who can independently make good judgments about when and how to operate. This philosophy has allowed us to meet our harvest budgets each year while also complying with BMPs, certification standards, and any special requirements of the WFCE.

What steps is Lyme Timber taking to shore up logger stability?

We don't have a single policy across our entire portfolio, but we try to be responsive to the needs of individual contractors in each region. During the 2009-2010 market downturn, we maintained harvest levels on New York and Tennessee properties at a time when many other landowners were pulling back. We also increased our fuel surcharge payments, which impacted our harvest margins, but helped keep contractors going through some difficult times. As markets have recovered we have had the infrastructure in place to benefit from higher margins.

Does Lyme Timber offer loggers long-term contracts or any type of financing assistance?

We have entered into long-term contracts with loggers and we may do more in the future. In many cases, however, there is enough trust in the relationship between the contractor and the forester that a long-term contract is not necessary.

Our preference is to let the banks do the financing. If the bank requires a longer-term commitment from us as part of the financing package, we are more than happy to consider it. My sense is that most established contractors have access to debt financing. The bigger issue is a stable work base and a profitable operating strategy.

Do you anticipate a continuing logging capacity shortfall going forward?

I don't think the sky is falling and there is a lot of regional variation. Where pulpwood markets have remained steady, I think logging capacity is less of an issue. In regions with weak pulpwood markets—parts of the Appalachian region, for example—we do anticipate a continued shortfall. Loggers have gone out of business and those that have survived have focused on cutting wood closer to home. In regions where there is not enough capacity, landowners are going to have to get used to paying higher rates if they want to increase harvest levels. We've had to factor higher rates into our investment underwriting in some regions. This may be one reason why we've been less successful at acquiring new properties in recent years.

In your opinion, what are the major issues confronting loggers today?

Again, it's hard to answer this without acknowledging the regional variations. But I think in many locations the major issue is business profitability and stability of work. Although fuel costs, workers compensation, health insurance, and other costs are all major factors, I see greater challenges on the revenue side of the ledger.

From my own contracting experience, I know that it's very hard to make more money solely by reducing costs. Most established logging contractors are already highly productive and efficient. There may be some opportunities to reduce financing costs and increase utilization with greater work stability, but there needs to be a sufficient profit margin to justify the investment. Owners of logging businesses are resourceful people and if they see a business opportunity they will figure out how to manage costs and maximize their chances for success.

Lyme Timber is the first TIMO to support the work of the American Loggers Council (ALC). What prompted that 2013 decision?

I met Danny Drueter at a conference and was impressed by his leadership. We shared a similar perspective on a number of issues, including the biggest challenges facing logging contractors. I have followed the ALC from afar for some time and generally want to support organizations that give contractors a voice and elevate their status as a profession and within the supply chain.

Every part of the supply chain needs to be healthy for the forest products industry in the U.S. to remain competitive.

Do you think other TIMOs should support ALC?

I think organizations, like us, that engage in service contracts with logging contractors should consider joining. However, in my view, it's important that the majority of ALC funding come from logging contractors or logging contractor associations. The organization should keep its focus on the issues that are most important to contractors.

From the standpoint of the logger, what are some of the positives/negatives that have evolved with the fundamental structural shift in timberland ownership and management since 2000 or so?

The "new" owners of timberland, the TIMOs and REITs, are managed independently of mills and the consuming side of the industry. One of the positives is greater flexibility to manage lands for long-term value and in some cases a greater willingness to focus on factors other than fiber cost. On the other hand, without a mill to supply, TIMOs and REITs may be less committed to maintaining the harvest levels necessary to keep contractors going during difficult times. The breakup of large industrial land bases into smaller, more fragmented ownerships creates another set of challenges for contractors. One of the benefits of working forest conservation easements is that they can keep some of

the large industrial forests intact.

What can the consuming side of the industry do to help strengthen the logging force?

Mills can do some of the same things we are doing. But probably the most important thing for mills to do is stay in business and invest in producing and marketing a better product. It goes without saying that strong mills and wood consumers are critical to the entire supply chain.

What can loggers do to help strengthen their businesses?

As with any business, communication and teamwork are two of the most important factors to success. The logging business owner needs to be able to communicate effectively with a wide range of people—employees, landowners, foresters, truckers, and mills.

It's also critical for logging contractors to understand their cost structure. Landowners and mills may be receptive to paying a little more, but they want to feel that there is a basis for doing so. I believe that contractors who understand their costs and can communicate effectively will find ways to make the business work. The entire supply chain depends on getting wood from the forest to the mill and there is an increasing recognition that contractors need to be profitable to stay in business. Contractors should be aware of this reality and look for landowner and mill relationships that are built on trust and mutual benefit.

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