

Gresham House Timberland LP

Interim Report
31 January 2024



Gresham House
Specialist asset management

Contents

01

Interim Report

Performance Summary	4
Forest Portfolio	7
Market Review & Outlook	11
Administration	14

02

Additional Information

The LP's Management Team	16
LP Information	17
Important Information	18



A landscape photograph showing a dense forest of evergreen trees on a hillside. In the background, there are rolling hills and mountains under a clear, bright blue sky. The overall scene is peaceful and natural.

01

Interim Report

Performance Summary

Executive summary

Gresham House Timberland LP (the LP) has experienced improved trading conditions during the six-month period to 31 January 2024. The UK timber market is showing signs of recovery resulting in slightly more competitive bids being received for the LP's timber. Operations are broadly in line with budget and the annual distribution is forecast to be paid in July 2024 as planned.

Trading performance

The Manager has produced unaudited Management Accounts for the LP for the six months ended 31 January 2024. The Report and Financial Statements for the full year to 31 July 2024 will be issued to Limited Partners by 31 October 2024.

Profit for the year from ongoing activities, net of expenditure, including restocking and overheads, is forecast to be £3.1mn, representing an increase of more than six times the £0.5mn profit for the previous financial year.

The forecast retained profit is £0.8mn (£0.3mn below budget), after payment of the planned £3.4mn distribution, but is contingent upon the two properties currently being marketed for sale achieving a profit of £1.1mn, in line with budget. In the event that acceptable offers are not received, the Manager will review the budget for the current financial year.

Forestry expenditure of £3.1mn and overheads of £1.8mn (including portfolio administration and woodland insurance) are expected to be broadly in line with budget.



A summary profit and loss table is provided below:

	2023-24 Budget (£mn)	2023-24 Forecast (£mn)	2022-23 Actual (£mn)
Total turnover	8.2	7.9	4.1
Operating costs	(3.0)	(3.1)	(1.9)
Administrative and other expenses	(1.8)	(1.8)	(1.6)
Net income	3.3	3.1	0.5
Interest receivable	0.1	0.1	0.1
Distribution	(3.4)	(3.4)	(2.0)
Profit on sale of forests	1.1	1.1	-
Profit/(Loss) after distribution and sale of forests	1.1	0.8	(1.3)

(Figures rounded to one decimal place)

Capital expenditure in the LP's forests is forecast at £1.9mn, £0.2mn below budget, with the balance relating to a roading project which has been deferred to the next financial year. This expenditure mostly relates to the construction of new roads required to access timber for planned harvesting. As noted later in this Report, the funding of capital expenditure is mainly due to be met by the sale of two non-cash generative properties.

Distributions

As was communicated in the 31 July 2023 Annual Report, for the year ending 31 July 2024 the Manager has rebased the distribution to the level it was in July 2021 (the last time it was paid in full), in order to deliver a sustainable cash yield whilst refraining from harvesting excessive amounts of timber. Increases of CPIH (as measured from 2024) +0.5% are proposed to apply from July 2025 onwards.

The distribution payable in July 2024 is therefore forecast to be £32.06 per Partnership Share, which represents an increase of 70.8% from the distribution paid in July 2023, of £18.77 per Partnership Share.

This payment, totalling £3.4mn, would result in all of the LP's forecast net income for the year of £3.1mn being returned to Limited Partners, with the balance being funded from brought forward profit and loss reserves.

The targeted payment of £32.06 per Partnership Share in July 2024 amounts to 1.8% of the July 2023 NAV. This remains in excess of the targeted distributions of between 1.0% and 1.6% of NAV across other mature Gresham House Forestry Funds with similar investment mandates.

Limited Partners should note that the General Partner retains discretion over the distribution and the final payment amount will be determined based on the financial position of the LP in July. The Manager will continue to review the situation and will update Limited Partners prior to the financial year end.

Partnership Shares in issue

Share class	Number of shares
Founder Partnership Shares	22,586
“B” Partnership Shares	14,880
“C” Partnership Shares	38,879
“D” Partnership Shares	28,885
Total	105,230

Gearing

The Manager will continue to actively manage the portfolio in order to maximise value. The LP has the ability to borrow up to 10% of NAV and the Manager might consider using gearing to acquire additional forest properties as appropriate, but the LP currently has no gearing.

Net Asset Value (NAV)

The LP’s NAV as at 31 July 2023 was £191.3mn, equating to £1,818.26 per Partnership Share.

An external valuation of the LP’s forestry portfolio will be conducted as at 31 July 2024 in accordance with RICS Global Valuation Standards. Recently, the forestry market has been quiet, with very few large-scale properties being marketed for sale. In the absence of comparable properties, other portfolios managed by Gresham House have recently seen modest decreases in valuations.

However, in the longer term, the Manager expects demand for UK forests to increase, with investors continuing to seek exposure to sustainable real assets. Forests are valued using long-term assumptions and short-term timber price volatility is not generally reflected in asset values, although the rise in market discount rates has impacted the required return from investments across almost all asset classes.

Macroeconomic update

Persistently high levels of inflation present in the UK economy have caused the Bank of England to maintain interest rates at current levels. There were 14 consecutive interest rate increases, from 0.1% in December 2021 to the current level of 5.25%, reaching the highest level for 16 years. The tightening in monetary policy, designed to reduce spending, has caused a reduction in demand for timber from housebuilders, which in turn has put downward pressure on the price being offered for the LP’s construction grade timber. Other grades of timber such as small roundwood have continued to generate reasonable levels of demand and generally acceptable prices, therefore the Manager’s overriding strategy has been to assess the suitability of the originally budgeted harvesting contracts and to adjust the offerings to best suit the market in terms of timber grade and geography.

It is encouraging to observe that the rate of UK inflation has decreased following these interest rate rises, as intended. The Manager is looking forward to the prospect of a phased reduction of interest rates in subsequent periods which, it is hoped, will help to stimulate demand from UK housebuilders.

Increases in cost of capital, uncertainties over future economic stability, and the wider impact of inflation are having fundamental effects on a wide range of asset classes. Whilst the alternative and real asset sectors are showing resilience, they are not immune. In terms of forestry asset values, timber prices are down (although now recovering), liquidity in the market is thin, operational costs are up and underlying discount rates have moved. In other sectors this might result in substantial forced sales and significant volatility in price, but on the basis that most UK forests are unlevered and privately held, forced selling is very limited. During 2023, Gresham House saw very few high quality large scale assets being offered to the market; trades that did occur tended to be small, or of a quality that sellers were less concerned over attaining peak prices.

As a result, Gresham House is seeing some downward pressure on values, which is very much quality and scale driven. Forestry has recently been through a very strong period of growth and value appreciation, in Gresham House’s opinion the long term value drivers have never been more relevant. Expectations for global timber demand remain intact, the drive to a lower carbon economy never more important, and the long term appetite for natural capital and sustainable investment increasing. An investment in forestry and timber should always be seen as a long-term investment, Gresham House remain confident that biological growth will continue to underpin returns, real timber prices will rise, and inflation protection will remain. These are the core drivers of long-term value and return.



Despite the challenges present in the macroeconomic environment, the Manager remains confident that the outlook for forest assets remains strong, primarily as a result of:

- rising demand for more sustainable materials, including timber for its decarbonising qualities;
- the ever-increasing interest in the asset class for its sustainable and diversifying characteristics;
- the requirement for the UK to increase the level of tree planting in order to meet net zero emissions by 2050;
- strong capital growth of the underlying land; and
- the defensive characteristic of the asset class, whereby timber harvesting can be timed to align with a receptive market or postponed, whilst the crop grows on in volume and value.

The Manager's strategy remains to manage timber price risk through carefully monitoring timber processor activity and market demand for different timber products, and tailoring offerings to the market to meet those demands, by either reducing or increasing harvesting based on market strength. The Manager is clear that selling the LP's timber into a depressed market is not in the long term interests of Limited Partners. This may impact the future distribution policy.

Forest Portfolio

Timber harvesting

From the timber sale contracts agreed during the financial year to date, the Manager has secured a blended timber price of £43.18, slightly below budget of £44.76.

Early in the financial year, the Manager had been pleased to receive confirmation of grant funding for a major road upgrade which would allow harvesting of the next planned coupes at two properties in west Scotland. However, unfortunately, the project was dependent upon the neighbouring landowner's involvement and, following their recent withdrawal from the process, the Manager is now having to seek alternative access arrangements. The Manager will continue to upgrade the road without grant funding, in line with the original plan for the asset, however the timing of this is such that total timber revenue forecast for the year ended 31 July 2024 is now £0.3mn less than was budgeted, with these coupes now not being expected to be accessible until the following financial year.

As a result of the delays to the roading programme at these two sites, the Manager is forecasting to generate 97% of the budgeted timber revenue. Overall, the harvesting contracts are forecast to produce c.169,000 tonnes of timber (2023: c.76,000) at an average timber price of £44.66 per tonne, generating timber revenue of £7.5mn (2023: £3.7mn).

A summary of the harvesting contracts (excluding thinning income) for the year to 31 July 2024 is shown in the table below.

At the point of publication, contracts had been agreed for c.122,000 tonnes of the c.169,000 tonnes forecast, such that 72% of the revised forecast timber income for the year has already been contractually secured.

The remaining contracts are in the process of being actioned.

2023-24	Hectares	Tonnes	Tonnes/ hectare	Blended £/tonne	Blended £/hectare	Total Revenue £mn
Budget	465.6	174,486	375	44.76	16,773	7.8
Forecast – contracts agreed to date	335.3	122,128	364	43.18	15,729	5.3
Forecast – contracts to be agreed	124.0	46,623	376	48.54	18,249	2.2
Forecast – total	459.3	168,751	367	44.66	16,410	7.5

Carbon offsetting

Carbon sequestration figures are calculated annually at the LP's year end.

The total carbon currently stored in the LP's forestry portfolio is estimated to be 2.7 million tonnes, equating to just under 26 tonnes per Partnership Share.

The total annual sequestration of carbon dioxide by the forestry portfolio is estimated to be c.95,000 tonnes (0.9 tonnes per Partnership Share) for the year ending 31 July 2024.

Average annual carbon dioxide emissions per capita in the UK were 4.7 tonnes in 2022¹, so ownership of just five Partnership Shares is the equivalent to the sequestration of the average annual carbon emissions produced by one person in the UK over the course of the year.

Acquisitions and disposals

As at 31 January 2024, the forest portfolio totalled 9,908 hectares, comprising 30 properties.

There were no property acquisitions during the period.

In line with the Manager's plan to rebalance the portfolio, during February Dalmally and Dunter Law were launched to the market, for sale by John Clegg & Co. Completion will be targeted for Q4 of the LP's financial year, which is in the 2024-25 tax year, subject to acceptable offers being received.

Both properties will be sold with restocking liabilities. Harvesting has nearly completed at Dunter Law and the final harvesting coupe at Dalmally has been sold. Following the completion of harvesting, these properties will have no mature timber remaining and would therefore not generate any revenue for the Partnership's remaining term. The majority of the proceeds from these sales will be reinvested into some of the remaining 28 assets to create and improve value enhancing infrastructure, which will allow the Manager to access further mature crops for harvesting and cash generation.

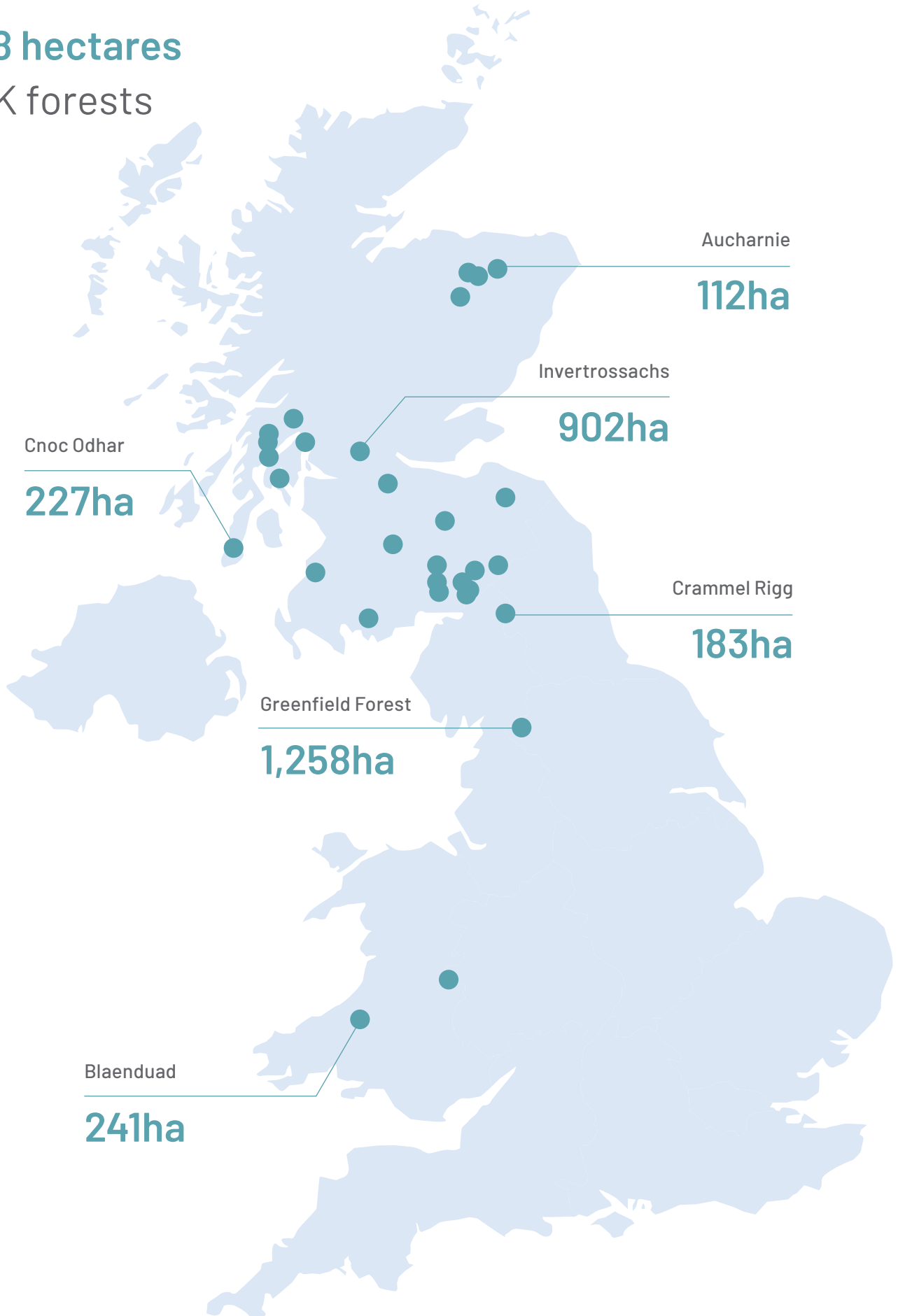
Relatively few opportunities to purchase high quality young forests have been seen within the market of late. The Manager believes that due to the shortage of such forests available for purchase, a strategic sale of these two assets in 2024 should maximise their value for the LP.

1. <https://www.statista.com/statistics/1299198/co2-emissions-percapita-united-kingdom/>



9,908 hectares

30 UK forests



Portfolio analysis

The forest portfolio comprises a total area of 9,908 hectares, of which 6,995 hectares (70.6%) is commercial crop area. This is either stocked with commercial crops or has recently been harvested and is due for restocking.

The commercial crop area currently consists of 84.0% Sitka spruce and 16.0% other conifer species, and land which is awaiting restocking.

The LP continues to hold significant reserves of mature timber, with 3,673 hectares of commercial crop over 30 years of age which, subject to separation requirements and market conditions, can be harvested as and when required to generate cash flow. The strategy is to prioritise harvesting of the oldest crops within the portfolio where appropriate.

The LP’s portfolio contains a significant land area, 29.4%, which is not core commercial conifer area. This land is largely retained as open ground. Open space within a forest is important, it breaks up the canopy of the woodland and allows light to reach the forest floor, with the gaps creating sheltered, warm patches that support wildlife. When combined with veteran trees and native broadleaves, these areas provide a sheltered ride network and ideal habitat for birds and bats.

The Manager is reviewing the potential uses and environmental benefits of the unplanted areas owned by the LP, with a view to maximising the economic, environmental and social benefits that these areas provide.

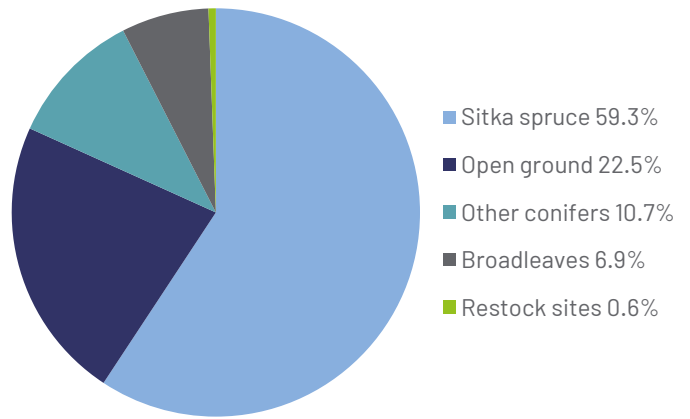
The portfolio comprises 6.9% native and mixed broadleaves. Native tree species, such as oak, rowan and cherry, are vital for the UK’s woodland ecosystems and biodiversity. Being the species that our wildlife evolved and adapted to rely upon, it is these trees which best provide our mammals, birds, invertebrates, fungi and mosses, with the habitats and food they need to thrive.

Under sustainable practice regulations such as UKWAS, a more diverse range of species will be introduced as the forests are restructured, to ensure a greater variety of species and to promote biodiversity across the portfolio.

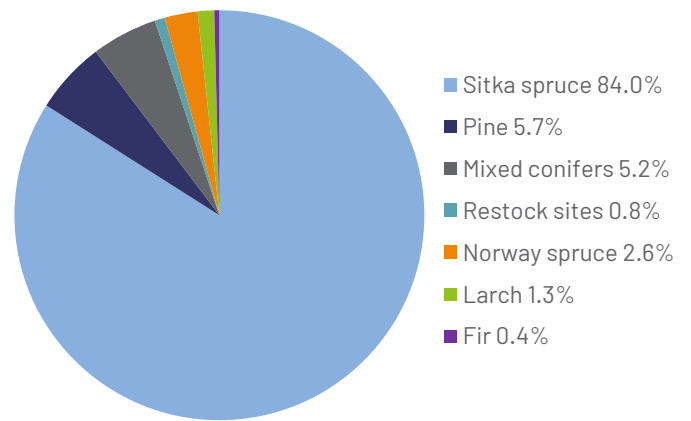
All forests owned by the LP are managed in accordance with Forest Stewardship Council (FSC) guidelines, which confirm that the forest preserves biological diversity and benefits the lives of local people and workers. The FSC accreditation also helps to maximise the timber prices paid for timber harvested from the LP’s portfolio.

The weighted average age of the commercial crop within the portfolio is 26 years, which is distributed as shown in the following bar chart.

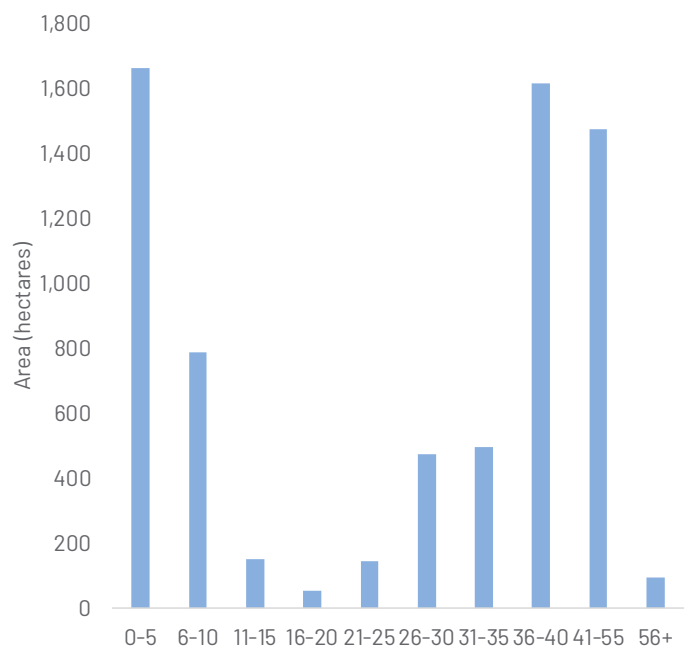
Portfolio area breakdown



Commercial crop area



Crop Age Distribution of Commercial Species



Market Review & Outlook

Global timber market review

- Demand for timber end products remains subdued but constraints on supply are creating some positive price pressure.
- Constrained timber supply and the housing shortage in the US means there is potential for a recovery in timber prices.
- Gresham House considers demand and price will likely improve during 2024, but that the extent will remain limited by the wider macroeconomic conditions.

The US lumber markets have remained steady through 2023. There has been some inertia in the US housing market, with many homeowners in the US having secured low remortgage rates on their existing homes and are consequently reluctant to move. However, demand for housing far outweighs supply with the gap estimated at 6.4million single family homes. There is therefore optimism that new housing activity will pick up, resulting in an increase in lumber demand during 2024. The housing market index rose 25% during the year to January 2024 and housing starts rose 18% in the month to November 2023. The wildfire season was the worst on record in Canada, further constraining the supply from the region which had already been hit by long term pine beetle damage. Rising demand in the US is therefore expected to see increased imports from Europe, creating positive price pressure there.

The war in Ukraine has isolated Russia from key timber trade partners. There has been a 20% drop in lumber production due to low investment and corporate divestment, as shown by Ikea selling its final asset in Russia at the end of 2023. Annual exports from Russia are expected to have fallen over 10 million m³ since the start of the conflict. This reduction has subdued the impact of poor demand for timber products in the western economies.

China's economy continues to grow with GDP up 5% year on year in 2023, but the rate of growth has slowed significantly from the 20-year average of 9%. Timber imports were 33% lower in 2023 than 2021 and at a similar level to those seen in 2012 and 2015. The order from a Hong Kong court to liquidate the holding company of Evergrande, the Chinese property giant, is likely to lower confidence and activity in the Chinese construction sector. This may subdue timber demand and prices.

China is the main export market for New Zealand, representing 80% of exports. New Zealand export prices fell 21% in the year to October 2023, although domestic demand is strong. Alternative export markets are opening up with steady demand from South Korea and improving export prices to India. Despite the relatively poor outlook for the Chinese export markets, in the short term, demand from China is expected to improve following the holiday season and price improvements were reported during Q4 2023.

In Australia, the market remained steady through 2023 but with a slowdown in December. Forest and Wood Products Australia have announced the launch of the softwood Timber Market Index. This has been developed with strong support from industry and is a collaboration between the Australian Forest Products Association and Forest and Wood Products Australia. The index will allow the tracking of price movements to support planning and decision making in the timber industry.

In Europe, poor demand for timber end products in line with the wider economic headwinds has seen the European Sawlog Price Index fall 12% in the year to Q3 2023. Timber prices have fallen, in line with the poor demand, notably in the Baltic states and central Europe. In 2018/19, drought induced beetle damage saw a significant increase in the harvest levels in Europe. One of the worst hit countries was Germany which became a net exporter of logs as a result. The beetle populations have normalised, resulting in a significant reduction in harvest levels, and it is expected that Germany will return to being a net importer of sawlogs in 2024. This slowdown in production in Germany will constrain the supply of sawlogs in Europe and is likely to create positive price pressure.

Although log exports from Sweden were 32% down in the year to September 2023, forest owners have seen log prices rise almost 12% and pulpwood prices increase by 37% in 2023. The aforementioned reduction in beetle damage to timber crops, combined with lower storm damage is allowing forest owners to choose to delay their felling. This has created further positive price pressure, despite relatively poor demand for timber end products.

Despite the macroeconomic headwinds reducing the demand for timber end products, Gresham House considers there is an opportunity for price improvements in 2024. Supply from the major producing regions of Canada and Russia is set to remain constrained, meaning that as timber demand stabilises, prices are likely to improve.

UK timber market review

- UK standing timber prices stabilised during Q4 2023.
- Timber end product prices are relatively strong despite poor demand.
- Demand for standing timber has recovered in early 2024 with price improvements reported.

The Gresham House real standing timber price index graph shows prices stabilised during Q4 2023. In real terms, prices fell 1.5% in South Scotland, 1% in Wales and rose 6% in West Scotland. Log prices held steady in Wales and South Scotland but rose 3% in the West of Scotland. Small roundwood prices were also steady with the seasonal increase in demand for biomass offset by production issues at major board processors. As there was an oversupply of standing timber, Gresham House reduced timber sales volumes in order to protect price.

The Builders Merchant Building Index shows that UK demand for timber end products remained flat during 2023. Poor weather, combined with the expected seasonal slowdown in construction activity, saw demand for end products fall during Q4 2023. The Construction Products Association report that housing activity in 2023 was down 19% compared with 2022 and forecast that it will remain steady in 2024.

The UK Structural Timber Price Index remained flat during 2023, and although back 43% from the market peak in August 2021, it remains over 10% ahead of the pre-pandemic levels. Given the relatively poor demand, this demonstrates the resilience of timber prices, although rising costs of production are putting processors under pressure.

The start of 2024 has seen improving demand as merchants replenish their stocks and this has resulted in some positive price movements. Sweden remains the main supplier of imported timber into the UK, and with rising roundwood prices, Swedish processors will look to increase sawn timber prices to protect their margins. Although, any improvement in prices is likely to be tempered by the low overall demand.

Gresham House further reduced standing timber sales during Q4 2023 in line with the production of UK processors. This helped to alleviate the oversupply of round timber seen during Q3 2023, and processors are now looking for new supply as merchants restock in time for spring. Standing timber sales in early 2024 have already seen improvements in sales prices and there has been a strong level of interest. Gresham House considers that prices for standing timber will continue to improve. Although, with significant volumes now coming to the market, the extent of that recovery is likely to be constrained.



Long-term global supply and demand

Increasing adoption of timber in construction in the UK is a key opportunity for the timber industry. The “Timber in construction roadmap” policy paper sets out the UK Government’s vision to grow support for new tree planting through promoting the use of timber in construction. Increasing the understanding of the carbon lifecycle will further enhance the role timber products have to play in decarbonisation. In addition, education on fire safety and durability of engineered mass timber systems is likely to see increased timber demand.

Please view our [New Growth in Timber Markets paper here](#).

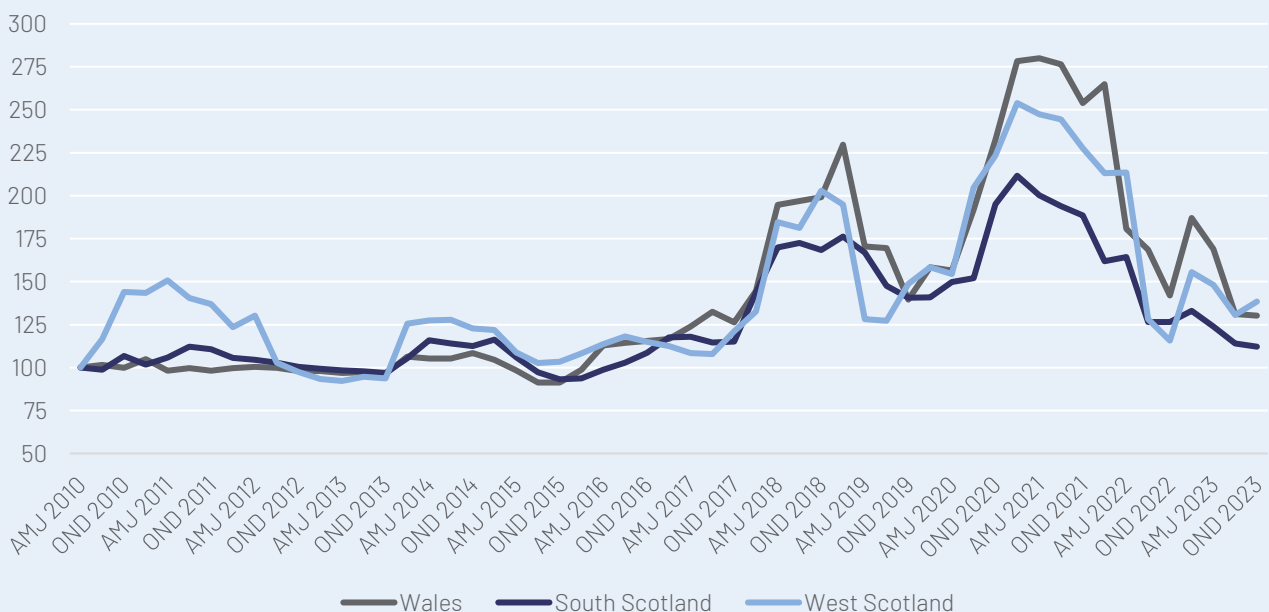
Gresham House expects global timber consumption to rise by 3.1% per annum over the next 30 years. This will continue to be driven by urbanisation, decarbonisation and increased housebuilding. The World Bank predict global timber consumption to quadruple over the same period, driven by economic and population growth.

Globally, most countries have set significant targets to reduce carbon emissions towards net-zero by 2050. Timber will play a critical part in this transformation. The dual effects of urbanisation and decarbonisation will lead to more new homes and cleaner low carbon intensity buildings being built from timber. Wood will increasingly replace high carbon intensive steel and concrete.

Rising demand for timber is set against a constrained supply due to the long rotation length of the trees and competition for land use. This supply demand imbalance will result in increased timber prices over the medium to long-term. Commercial forestry remains an excellent diversifying investment, uncorrelated to other asset classes, offering inflation protection. It is underpinned by income from timber sales and the biological growth of the trees.



Gresham House Standing Timber Prices - Real Index*



*(excluding impact of inflation)

Source - Gresham House data. The index is based on the standing prices calculated from the highest end product prices evidenced in Gresham House timber sales during the quarter. The standing prices assume consistent working/haulage costs and crop quality to show a transparent view of the effect of the market movements.

Administration

Manager's strategy

The strategy is to maximise the total return to Limited Partners, selling timber at appropriate prices in order to cover operating costs and provide an element of income via distributions to Limited Partners.

Fund Management team

As at the LP's upcoming year end, Anthony Crosbie Dawson will replace Olly Hughes as Fund Director and will in turn be replaced as Fund Manager by Emma Woolley.

Additions to Limited Partners' holdings in the LP

Limited Partners have the opportunity to increase their holding in the LP by acquiring secondary shares which are offered for sale. As existing Limited Partners, the Manager is advised that any additional share purchases in the LP should immediately qualify for 100% inheritance tax relief without a two-year qualifying period, providing their percentage ownership in the LP does not significantly increase. Existing Limited Partners may bid for any number of shares to add to their holding, there is no minimum.

The Manager markets shares being sold by existing Limited Partners for a period of two weeks. These can be accessed using this link <https://greshamhouse.com/current-shares-for-sale/>. Bids can be received by post or by email to admin@greshamhouse.com and should detail the number of shares the bid is for and the price per share offered. The Manager presents all valid bids to the vendor following the closing date and will inform bidders on whether their offer is successful or not once the vendor has informed the Manager of their decision. Successful bidders will be sent completion documents and a payment request, with payment due within two weeks of the closing date.

Further details of current and future sales are available by contacting Gresham House at sharetransactions@greshamhouse.com or 01451 844655.

Liquidity

During the six months to 31 January 2024 a total of 324 Partnership Shares were sold (c.0.3% of the total shares in issue), with the Manager arranging deals between vendors and purchasers.

The weighted average sale price was £1,673.91 per Partnership Share, c.7.9% below the published NAV of £1,818.26 as at 31 July 2023.

LP Termination Dates

The LP has an Initial Termination Date of 31 July 2032 and a Final Termination Date of 31 July 2040.

Taxation

The Manager expects to issue Taxable Income Statements for the Tax Year 2023-24 to Limited Partners in July 2024.

Website administration

Limited Partners and their IFAs are able to view the latest annual valuation via the Client Portal. If you have not already obtained a password, please follow this link to complete the registration process:

<https://secureclientportal.greshamhouse.com>

Client satisfaction

Please do not hesitate to contact a member of the Gresham House Asset Management team if you wish to discuss your investment or provide any feedback on this report. Gresham House are committed to ensuring that the needs and expectations of our clients are met at all times and would therefore welcome any suggestions to improve our service delivery.



Anthony Crosbie Dawson

Fund Manager

On behalf of Gresham House Asset Management Limited, Manager

25 March 2024



02

Additional
Information

The LP's Management Team

Please do not hesitate to contact a member of the management team if you wish to discuss your investment or provide any feedback on this report. Gresham House are committed to ensuring the needs and expectations of our clients are met at all times and would therefore welcome any suggestions to improve our service delivery.

Please see the website for more details on the team's professional experience:
www.greshamhouse.com/our-team



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Important Information

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