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RYN - Q4 2017 Rayonier Inc Earnings Call

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OVERVIEW:

Co. reported 4Q17 sales of $240m and net income attributable to Co. of $64m or $0.50 per share. Expects 2018 net income attributable to Co. to be $78-87m.

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PRESENTATION

Operator

Welcome, and thank you for joining Rayonier's Fourth Quarter 2017 Teleconference Call. (Operator Instructions) Today's conference is being recorded. If you have any objections, you may disconnect at this time.

Now I will turn the meeting over to Mr. Mark McHugh, Senior Vice President and CFO. Sir, you may begin.

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Thank you, and good morning. Welcome to Rayonier's investor teleconference covering fourth quarter earnings. Our earnings statement and financial supplement were released yesterday afternoon and are available on our website at rayonier.com.

I'd like to remind you that in these presentations, we include forward-looking statements made pursuant to the safe harbor provisions of federal securities laws. Our earnings release and Form 10-K filed with the SEC lists some of the factors that may cause actual results to differ materially from the forward-looking statements we may make. They're also referenced on Page 2 of our financial supplement.

Throughout these presentations, we'll also discuss non-GAAP financial measures, which are defined and reconciled to the nearest GAAP measure in our earnings release and supplemental materials.

With that, let's start our teleconference with opening comments from Dave Nunes, President and CEO. Dave?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Thanks, Mark. Good morning, everyone. First, I'll make some overall comments before turning it back over to Mark to review our financial results, then I'll ask Doug Long, our Senior Vice President for U.S. operations, to comment on our U.S. timber results. I'll cover the New Zealand Timber results. And following the review of our 3 Timber segments, Chris Corr, our Senior Vice President of Real Estate, will discuss our Real Estate results.

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We're very pleased with our fourth quarter results and full year results. For the full year, we achieved adjusted EBITDA of $291 million, well ahead of our prior guidance and an increase of 21% over the prior year adjusted EBITDA.

And once again, the quality of our assets and markets, the diversity of our portfolio and the dedication of our employees allowed us to achieve strong overall results, despite some continued pricing headwinds in the U.S. South.

Full year adjusted EBITDA in the Pacific Northwest Timber segment increased 56% versus 2016, while full year adjusted EBITDA on the New Zealand Timber segment, excluding the impact of a $24 million land sale in the second quarter, increased 46% versus 2016.

Both the Pacific Northwest and New Zealand Timber segments benefited from strong price gains during the year, which had continued into the early part of 2018.

In our Southern Timber segment, we continued to enjoy relatively strong pricing in our coastal Atlantic markets, where supply/demand dynamics are generally more favorable than the broader U.S. South. However, those positive market dynamics were offset by both regional mix and lower-priced salvage volume from both fires and hurricanes during the year, resulting in a slight decline of just over 1% in our full year adjusted EBITDA for the Southern Timber segment.

Real Estate adjusted EBITDA declined by 16% year-over-year, driven by 33% fewer acres sold due to the 18,000-acre Townsend Bombing Range transaction in 2016. However, our average price per acre on real estate sales increased by 43% to just over $3,700 per acre as we continue to focus on extracting maximum value from our HBU portfolio.

I am very proud of how well our team worked together amid some challenging market conditions to generate strong 2017 results, and I remain optimistic about the market environment as we look into 2018.

We've continued to see steady growth in single-family construction, which is a key driver of wood products' demand and ultimately timber demand. In 2017, single-family starts increased roughly 9% over 2016 levels, and we're expecting similar growth in 2018.

We've further seeing the export markets and China, in particular, play an increasingly large role in the global demand for wood fiber. We've already seen this trend contribute to a significant tightening of the supply/demand balance in both the Pacific Northwest and New Zealand Timber markets, and we're optimistic about the prospects for further growth in our log export business from the U.S. South.

We believe that Rayonier is uniquely positioned to capitalize on these trends given the geographic footprint of our portfolio and our proximity to ports as well as our pure play focus on highly productive softwood timber lands.

Within our Real Estate segment, we're also very encouraged by the strong pricing and steady demand for rural HBU parcels as well as the traction we're realizing on our Wildlight development project North of Jacksonville. Together these have translated into significant growth in our premium realizations over the last 2 years, as we continue to find innovative ways to unlock HBU value within our portfolio.

And with that, let me turn it back over to Mark to review our financial results.

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Thanks, Dave. Let's start on Page 5 with our financial highlights. Sales for the quarter totaled $240 million while operating income was $80 million and net income attributable to Rayonier was $64 million or $0.50 per share.

Our pro forma net income for the quarter, which excludes the [$39 million] (corrected by company after the call) gain off from a large disposition, was $25 million or $0.20 per share.

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Fourth quarter adjusted EBITDA of $77 million was 48% above the prior-year quarter due to strong performance in our Pacific Northwest Timber, New Zealand Timber and Real Estate segments, which was partially offset by reduced harvest levels and lower pricing in our Southern Timber segment.

On the bottom of Page 5, we provide an overview of our capital resources and liquidity at year end as well as a comparison to the prior year. Our cash available for distribution, or CAD for the year, was $189 million, which represents an increase of $44 million or 31% versus the prior year CAD. A reconciliation of CAD to cash provided by operating activities and other GAAP metrics is provided on Page 8 of the financial supplement.

We closed the year with $113 million of cash and roughly $1 billion of debt. Our net debt of $916 million represented 18% of our enterprise value based on our closing stock price at year-end. Note that these figures exclude $59 million of cash proceeds from Timberland and HBU sales that are currently held by LKE intermediaries and therefore, classified as restricted cash.

I'll now turn the call over to Doug to provide a more detailed review of our U.S. Timber results.

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

Thanks, Mark. Good morning. Let's start on Page 9 with our Southern Timber segment. Adjusted EBITDA in the fourth quarter of $20 million was $5 million and $1 million unfavorable to the prior quarter and the prior year quarter, respectively.

Fourth quarter harvest volume of approximately 1.2 million tons was 134,000 tons lower in the prior quarter and 63,000 tons lower than the prior year quarter. As communicated during our third quarter earnings call, we expected a slight decrease in fourth quarter harvest volumes due to wet ground conditions.

Fourth quarter pine pulpwood stumpage prices of $15.16 per ton were 7% and 4% unfavorable compared to the prior quarter and prior year quarter, respectively. Pine sawtimber stumpage prices of $24.44 per ton were 6% and 9% unfavorable compared to the prior quarter and the prior year quarter, respectively.

The decline in both pulpwood and sawtimber prices was primarily due to geographic mix. Specifically, in the fourth quarter, we had a large lump sum timber sale in Arkansas, which is our weakest market from a pricing standpoint. Excluding the impact of this sale, pine pulpwood and sawtimber prices would have been up slightly versus Q3.

With our Southern Timber holdings spread over 9 states and with the development of significant price differentials across regional submarkets, geographic mix will continue to be one of the biggest drivers impacting our average pricing on a quarter-to-quarter basis.

Full year adjusted EBITDA in the Southern Timber segment totaled $92 million versus $93 million in the prior year. Given the challenge of having to contend with 280,000 tons of salvage volume from both hurricanes and fires at significantly lower pricing during the year, I'm pleased with our overall results for the year and believe we are well positioned for a stronger 2018.

Now moving to the Pacific Northwest Timber segment on Page 10. Adjusted EBITDA of $11 million was $3 million favorable to both the prior quarter and prior year quarter. Fourth quarter harvest volume of 321,000 tons increased 27% relative to the prior quarter, but decreased 10% relative to the prior year quarter. The variances in quarterly volumes were generally due to weather and the timing of stumpage sales, and were additionally impacted by the decision to defer 50,000 tons of planned volume in Q4 to capitalize on the strengthening markets as we move into 2018.

Pulpwood prices of $44.44 per ton were 7% and 12% favorable compared to the prior quarter and prior year quarter, respectively. The favorable pricing variance was primarily due to geographic mix and competition from a growing market for chip exports going to Japan.

Sawtimber prices of $95.34 per ton were 6% and 27% favorable to the prior quarter and prior year quarter, respectively. The significant increase in sawtimber prices was driven by strong export markets to both China and Japan, coupled with a very competitive domestic market. Restrictions during the summer fire season exacerbated an already tensioned wood basket in the Pacific Northwest. Even after these fire restrictions were lifted,

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supply seemingly struggled to keep pace with demand, setting up an environment that was very favorable for log prices through the end of the year.

Full year adjusted EBITDA in the Pacific Northwest segment totaled $33 million versus $21 million in the prior year, as we benefited from a full year contribution from our 2016 Menasha acquisition as well as significant price increases during the year. Across our Southern and Pacific Northwest Timber segments, nontimber revenue totaled $6 million in the fourth quarter, an increase of $1 million compared to the prior year quarter. For the full year, nontimber revenue of $25 million was up $4 million or 20% over the prior year due to growth in our hunting and recreation, fill dirt, minerals and other nontimber income businesses.

Now Dave will review New Zealand Timber results. Dave?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Thanks, Doug. Page 11 shows the results and key operating metrics for our New Zealand Timber segment. Our New Zealand Timber segment delivered another strong quarter. Adjusted EBITDA of $23 million was $5 million favorable to the prior year quarter, primarily due to higher harvest volumes and increased export and domestic sawtimber prices and $6 million unfavorable compared to the prior quarter, primarily due to lower harvest volumes.

Export sawtimber prices increased 2% and 11% compared to the prior quarter and prior year quarter respectively, due primarily to continued strong demand from China. Domestic sawtimber prices in U.S. dollar terms were flat compared to the prior quarter and 7% higher than the prior year quarter as a result of continued strong demand for construction materials, partially offset by a modest decrease in the New Zealand dollar to U.S. dollar exchange rate.

Full year adjusted EBITDA in the New Zealand Timber segment totaled $109 million versus $58 million dollars in 2016 driven by higher volumes and higher pricing as well as a $24 million contribution from a land sale in the second quarter of 2017.

In our Trading segment, full year adjusted EBITDA was $5 million, more than double the prior year. In the fourth quarter, volumes increased 2% and average prices increased 8% compared to the prior year period, also due to stronger demand from China.

I'll now turn it over to Chris to cover Real Estate.

Christopher T. Corr - *Rayonier Inc. - SVP of Real Estate & Public Affairs and President of Raydient Inc*

Thank you, Dave, and good morning, everyone. As highlighted on Page 12, our Real Estate segment delivered solid financial results in 2017, including a very strong fourth quarter. Excluding large dispositions, real estate sales for the year totaled $88 million on 23,823 acres sold at an average price of $3,700 per acre. Fourth quarter sales, excluding large dispositions, totaled $33 million on 7,475 acres at an average price of $4,378 per acre.

Sales in our Improved Development category reflect the progress made on our Wildlight development project. Fourth quarter sales totaled $6 million, which included a mix of commercial and residential properties in Wildlight, totaling 22 acres at an average price of $295,000 per acre.

Commercial sales included parcels for a multifamily apartment complex, a bank and a health care campus, all of which are expected to drive interest in and traffic to the community. Fourth quarter closings also included 8 single-family lots. We continue to be pleased with our progress in Wildlight and the pipeline of opportunities as we head into 2018.

The rural category yielded sales of $3 million on approximately 1,200 acres at an average price of $2,721 per acre. Market interest in our rural properties remains positive, with per acre pricing comparable to the prior quarter and prior year quarter.

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Finally, in the nonstrategic and Timberlands category, sales totaled $23 million, driven by 2 significant transactions in Florida, at strong market premiums including 4,000 acres for $3,650 per acre and 1,922 acres for $4,000 per acre.

I'll now turn the call back over to Mark.

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Thanks, Chris. Before we discuss guidance, I wanted to highlight a change that we've made with respect to how we report nontimber income. In an effort to report certain revenue and expenses in a manner more representative of activities that constitute ongoing central operations, and in order to streamline our disclosure in preparation for the implementation of new revenue recognition standards in 2018, we reclassified nontimber income from other operating income net to sales and cost of sales. This reclassification applies to all nontimber income including lease and license income, carbon credit sales, log agency fees and other ancillary revenue streams. A reclassification was applied retrospectively to all periods presented in our fourth quarter earnings release and will be reflected in our 2017 Form 10-K. Please note that this reclassification had no impact on our historical reported adjusted EBITDA, operating income or net income.

Now moving on to guidance for the year. Page 14 shows our financial guidance by segment for 2018, and schedule G of our earnings release provides a reconciliation of this adjusted EBITDA guidance to net income attributable to Rayonier.

As we look to 2018, we continue to see overall positive momentum in our Timber segments as well as attractive opportunities to unlock value from our higher and better used real estate portfolio. While the U.S. South continues to experience a relatively slow recovery in sawlog prices, we still believe longer-term trends remain positive, and we are encouraged by the amount of wood products capacity expansion planned for the South over the next 2 years.

In 2018, we expect some modest price improvement in certain regional markets, but we expect the overall pricing in the Southern Timber segment to be relatively flat to 2017 average pricing due to geographic mix. Further, we anticipate an increase in harvest volumes to a range of 5.8 million to 6 million tons based on a full year contribution from our 2017 acquisitions in Florida, Georgia and South Carolina.

Overall, we expect our Southern Timber segment will contribute 2018 adjusted EBITDA in the range of $102 million to $107 million.

In our Pacific Northwest Timber segment, we expect a modest increase in harvest volumes to a range of 1.3 million to 1.4 million tons as well as higher sawtimber prices relative to 2017 average pricing, which we expect will yield 2018 adjusted EBITDA of $38 million to $42 million.

In our New Zealand Timber segment, we expect a modest increase in harvest volumes to a range of 2.5 million to 2.7 million tons as well as continued strong pricing dynamics, which we expect will yield 2018 adjusted EBITDA of $89 million to $95 million.

Our Real Estate strategy will continue to focus on unlocking the long-term value of our HBU portfolio. We currently have a strong pipeline of identified HBU opportunities as we look into 2018 including additional sales in our Wildlight development project. Overall, we expect real estate will contribute 2018 adjusted EBITDA of $78 million to $80 million, although we continue to expect that quarter-to-quarter results will be lumpy.

In total, we anticipate 2018 consolidated adjusted EBITDA of $280 million to $305 million, and net income attributable to Rayonier of $78 million to $87 million. Details on other elements of our financial guidance, including CapEx, DD&A, noncash basis of land sold, interest expense, taxes and minority interest are provided on Page 14 of the financial supplement and schedule G of the earnings release.

I'll now turn the call back to Dave for closing comments.

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David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Thanks, Mark. 2017 was another very busy and productive year for Rayonier, and I wanted to take a moment to recap some of the key milestones we achieved in executing on a number of our strategic priorities. In March, we announced that the company had entered into 3 transactions to acquire approximately 95,000 acres of high-quality timberlands located in coastal Florida, Georgia and South Carolina, which subsequently closed for a final purchase price of $214 million or roughly $2,250 per acre.

These properties were highly productive lands located in the top 3 markets in the U.S. South, which allowed us to upgrade our portfolio and build additional scale in a core operational region for Rayonier. Concurrent with this announcement, we also executed an overnight equity offering of 5.75 million common shares, raising $152 million of net proceeds, which was used to partially fund the acquisition purchase price. This was Rayonier's first ever follow on public offering, and we were pleased to have been able to deploy the proceeds into a transaction that was highly strategic for Rayonier and that we believe will be value accretive for our shareholders over time.

2017 was also a breakthrough year for our Improved Development business as we made significant progress on the initial infrastructure investments within our Wildlight project and also realized our first sales of both residential and commercial properties within the project footprint.

Over the summer, we completed construction of our new headquarters facility and successfully moved more than 150 employees into the new building, consolidating 3 leased offices into 1 building. We continue to recognize significant efficiencies, improved communication and a stronger organizational culture as a result of our office move. Our new headquarter's building has also served as a cornerstone for the Wildlight project, demonstrating our commitment to economic development in Northeast Florida where Rayonier has significant land holdings.

Subsequent progress on Wildlight during 2017 included the selection of 2 homebuilders for the project, the announcement of an alliance with University of Florida Health to construct health and fitness facilities within the project, and an announcement that Florida Public Utilities plans to relocate its headquarters to Wildlight on a parcel adjacent to Rayonier's headquarters building.

During the course of the year, we also remained very active with respect to our portfolio management efforts. In addition to our large acquisition in the South in the first quarter, we executed on a number of small bolt-on transactions across all 3 of our Timber segments. We also sold approximately 50,000 acres of large dispositions, totaling $95 million, including the sale of [24,645 acres] (corrected by company after the call) in Alabama in the fourth quarter for $53 million or $2,167 per acre.

We have a mindset of never being satisfied with our portfolio and are always looking for opportunities to either upgrade our portfolio through acquisitions or redeploy the proceeds from large dispositions in the capital allocation opportunities that will enhance our long-term value per share.

Over the last 3 years, we focused on creating a spirit of teamwork and culture of accountability and excellence throughout the organization. I believe that the culture we are reinforcing within our organization has resulted in greater coordination and collaboration, allowing Rayonier to be more nimble and proactive as our markets change.

Overall, we're very pleased with not only our financial results in 2017, but also the actions our employees are taking to build long-term value of our company.

In summary, we continue to actively seek out ways to improve both our organization and our portfolio. Our capital allocation strategy and operational philosophy are both intended to be nimble, flexible and opportunistic. As we've demonstrated over the past year, we will shift our priorities as needed to capitalize on the best available opportunities to maximize long-term value for our shareholders.

I'd now like to close the formal part of the presentation and turn the call back to the operator for questions.

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QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will come from Ketan Mamtora with BMO Capital Markets.

Ketan Mamtora - *BMO Capital Markets Equity Research - Analyst*

Congrats on a very strong year in New Zealand.

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Thanks.

Ketan Mamtora - *BMO Capital Markets Equity Research - Analyst*

First question, can you talk a little bit about what you are seeing with sawlog prices, both in Pacific Northwest and New Zealand thus far in 2018?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

You going to touch on the Pacific Northwest?

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

Sure. I'll be happy to start with that. As I mentioned in our comments, we saw the strengthening market going into 2018 and really, a supply that's starting to equalize out with demand, but we still think underlying there's good fundamentals with the growth in lumber demand and things like that. So we've seen strength that we believe will carry past our 2017 results.

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Yes. And Ketan, I think, also, it's important to recognize that for the Pacific Northwest in particular, you have a mix of the domestic market and the export market, and I think both of them right now are quite strong. And so that's part of why you're seeing the strong pricing as we finish the year and started into this year. And I also think, as we mentioned in our formal remarks, we had some supply constraints that have also exacerbated that.

Moving to New Zealand. Recognizing that New Zealand competes in the Pacific rim markets a little differently and in different parts of China as well as India and South Korea, you've got strong market conditions in export markets, while at the same time, we continue to see strong domestic market. So it's really a continuation of the market conditions we experienced this last year and recognize that there generally are not incremental sources of supply in New Zealand. So it's added additional price tension to those markets. But I think, as was the case with the Northwest, you've got, really, the combination of strong export and domestic markets occurring at the same time.

Ketan Mamtora - *BMO Capital Markets Equity Research - Analyst*

Got it. And that's very helpful, Dave. And just thinking with New Zealand for one more second. How is the strength in this market and the positioning that you talked about in terms of China and strong domestic demand? Has that changed your thinking at all, around the size of your presence in that market?

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David L. Nunes - *Rayonier Inc. - CEO, President and Director*

I think we've always been very bullish on New Zealand. It was certainly one of the reasons that we did our capital restructuring a few years ago, where we infused capital into New Zealand to pay down debt. We have grown modestly within New Zealand, but recognize there's the deal flow there is more limited than it is in the U.S. But we have continued to find small bolt-on acquisitions that we've been successful in, and we will continue to look for opportunities to grow our footprint there, because we like being in that market, both from the perspective that it's a highly productive area for softwood growing, its proximity to markets and its unique way of competing in those markets and the lack of correlation in pricing relative to our U.S. market. So from a portfolio construction standpoint, we think that's important as well.

Ketan Mamtora - *BMO Capital Markets Equity Research - Analyst*

All right. That's helpful. And then, just turning to U.S. now with my final question. Do you still think that 1.3, 1.4 million housing starts is about where the inflection point is for Southern log pricing? Or has been or there has been any rethink around that? Or maybe in terms of just lumber consumption in the U.S. South? Any thoughts there will be helpful.

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

I think the message that we have been trying to communicate with investors is, it really depends on the market that you're in, and recognize that the U.S. South really consist of a series of smaller markets. And we believe that there are subsets within the South, particularly today in that Atlantic coastal region, where we are essentially at a fairly tensioned market, where we see price elasticity such that when we have changes in lumber prices, we see that translate more rapidly into changes in log prices. Whereas in other parts of the U.S. South, we're not seeing that as much. We believe that the inflection point in some of the softer markets in the U.S. South is probably above the 1.5 million housing start level. So there will be parts of the U.S. South where you probably won't see meaningful price increases for a couple of years.

Operator

Our next question comes from Mark Weintraub from Buckingham Research.

Mark Adam Weintraub - *The Buckingham Research Group Incorporated - Research Analyst*

Maybe first, because it Doug, help us with your comments right at the end there, about getting to 1.5 million for certain markets in the U.S. South. What are you seeing on the M&A landscape? And with implications of rising interest rates, how is that affecting people's thinking as well do you think?

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

Yes. There's a lot that there are certainly, on the M&A front, there has been some press about how 2017 was a smaller year from a deal flow standpoint. But recognize there's still quite a bit of opportunities out there. We see a fairly active pipeline, but recognize as well that it's a variable quality and variable markets. And so we have tended to take an approach that's fairly choosy in terms of which areas we go into. We are always looking at getting into areas that have strong markets, and we're less likely to go into areas with markets that we feel aren't as fundamentally strong. And so we're continuing to see movement there. As it relates to interest rates, recognize that in a rising interest rate environment, that's going to be a byproduct of inflationary pressures. And those inflationary pressures are really going to translate to higher product value. So we some offset there in terms of our product pricing. And so we see it more as an impact as it relates to capital flows coming into the market and influencing the competitive environment for timber. And I think today, notwithstanding the expectation for rising interest rates in the near term, we're continuing to see plenty of capital out there on both the public and private side going after transactions.

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Mark Adam Weintraub - *The Buckingham Research Group Incorporated - Research Analyst*

And I guess, this is a follow-up, and maybe this is asking you to have more of a crystal ball then is reasonable. But certainly, in the U.S. South, the markets have already been factoring pricing improvement, and so while I certainly acknowledge your comments that higher interest rates are likely indicative of inflation et cetera and so, that those prices would go up. How does it play out when there already were expectations of inflation? Does that make the rising interest rates become potentially more of a depressant? Or do you think that people will just would say, "You know what? The increases in pricing are going to be even better than what we had previously thought?"

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Yes. Mark, this is Mark. I think a lot goes into that. And one point that I'd make there. I think as we underwrite Timberland acquisitions, there's not an uniform view around pricing. And I would say, you know, some of these market factors that we think about, as we look at the relative attractiveness of submarkets within the South can also factor into that long-term price expectation. And look at -- if you look across markets, we've seen some markets down significantly in the last decade relative to the last housing boom, and we've seen some markets relatively flat at that. Not on sawtimber prices specifically, but just on that composite price, because we have seen some offsetting growth in pulpwood prices. And so, if you're assuming kind of a 5-year reversion to trend line prices, that's going to imply a very different level of price growth in some of those more depressed markets than it will, and to say the coastal Atlantic markets in which a lot of our lands are located. So that was one of the points that we made at our Investor Day is that, yearly, we kind of pay attention to the different components of where you're expecting to get your return from and the different levels of risk associated with those components. But clearly, real price growth is a higher component of risk as you look at that total return. And so that's why we certainly like to be into strong markets where with good biological growth as well as on good, kind of, supply demand dynamics today as opposed to kind of forecasting that 5, 10 years into the future.

Mark Adam Weintraub - *The Buckingham Research Group Incorporated - Research Analyst*

Okay, makes sense. And on the real estate side. Obviously, fourth quarter, very strong. And I think a good deal stronger than what had been embedded in guidance, if I'm not mistaken. And so just wanted to get a little bit of an understanding as to whether that was primarily just a timing just a question of timing or whether or not there have been some changes in the market that make it better, stronger, different than what you may be had been thinking previously?

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

You know Mark, I'd say we're definitely encouraged by the trends the broad trends that we're seeing in that market. We've experienced some really good wins in 2017. Our pipeline for 2018 looks very strong. And if you just kind of look at those price realizations that we've been able to achieve in the Real Estate segment, they're meaningfully higher than what we've seen in the last 5 years. And so, again, we're I'd say we're encouraged and optimistic about that. It's hard to make very broad comments about the real estate business because they again, we try to be very opportunistic in that business. And a strong quarter doesn't necessarily imply that the next quarter is going to be an equivalent to that. Invariably, there's going to be some lumpiness in that business. And you going into the year, we certainly exceeded our expectations for real estate because we saw some pickup in demand, but it was also driven by a handful of larger transactions. And so I'd say that we're generally encouraged. I don't think that our fundamental view on that business long term has changed. We were always going to look to monetize somewhere in the range of 1% to 1.5% of our land base into that HBU market. But what we've emphasized in the past is really in terms of your ability to realize incremental cash flow and return on that business, it's all about premium. And so what we're doing now is, and what we've been doing for the last few years is really try to focus on building the pipeline of high value HBU opportunities. And it's exactly what we're doing with this Wildlight development project. We've always talked about that as a means to catalyze HBU value in this Northeast border region, where we own a lot of land. And so we're going to continue to do that. And again, we're certainly pleased with the results we achieved in 2017 and very optimistic about our outlook for 2018.

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Mark Adam Weintraub - *The Buckingham Research Group Incorporated - Research Analyst*

Great. And then lastly. Obviously, you were less directly impacted by changes in the tax code and some other sea corps et cetera. But as you look at your business, et cetera, are there some implications, strategic financial, that are worth highlighting related to the tax reform?

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

I think it's as much about our the impact on our downstream customers. And I think that you're going to probably see this translate into more of a willingness to make investments in some of the manufacturing capacity, particularly in the U.S. South, and we see that ripple effect coming through with added demand over time. So it's I'd say it's more of an indirect impact as well as, you know, in thinking about it from say, a real estate standpoint, the impact on the housing demand component from a development like a Wildlight.

Operator

Our next question comes from Collin Mings with Raymond James.

Collin Philip Mings - *Raymond James & Associates, Inc., Research Division - Analyst*

I wanted to go back to New Zealand for a minute. I'm just curious, any thoughts on valuations or readthroughs from the Nelson Forests' 141 plantations transaction that was announced in the region in December?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Yes, Colin. The transaction value hasn't been announced on that, and it probably won't be until they've completed their overseas investment office approvals, which are probably going to take place at some point this year. That was a very high quality asset in a very concentrated footprint. And so it certainly will be a comp that we will look at. I would say that pound-for-pound, our ownership there is a lot more scattered, and so that's a favorable aspect relative to the Nelson assets. But certainly, the interest that we saw in that asset is indicative of the capital flows that are trying to find a home in the New Zealand Timber space.

Collin Philip Mings - *Raymond James & Associates, Inc., Research Division - Analyst*

Okay, that's helpful. And then, just as we think about operations in New Zealand. Just as you're entering 2018 in terms of competition, are you concerned about competition from any other markets, whether it'd be Europe or South America, competing with some of the, I would argue, maybe a little bit unique end markets you guys serve there? Anything else you're seeing from either competition or a margin pressure standpoint in New Zealand?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Yes. I mean, working backwards on that question. I think one of the issues in New Zealand is has been that, every land owner is trying to capitalize on these markets. And so you've got a lot of increasing competition for contracting crews. We have addressed that through longer-term contracts, particularly on the harvesting and trucking side, to try to assure that our sources of volume are able to move to market opportunities. As it relates to the other part of your question, with respect to competition from other regions, I think recognize that New Zealand is very well-situated from a logistics standpoint to serve the markets that it's in. It has the dominant position in South Korea. It's got a very strong position, particularly in Southern China, and a growing position in the market in India. And I think, in all 3 of those markets, it competes uniquely, and it's really not the last increment of supply. And so that's why I think you tend to see more of those marginal effects is when you are that last increment of supply. I think we're very much a base load part of the volume in all those markets.

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Collin Philip Mings - *Raymond James & Associates, Inc., Research Division - Analyst*

Okay. And then, Mark, maybe turning to just the capital allocation for a minute. Given the continued improvement in cash flow. Just how are you approaching the dividend? Are there specific things the board's looking for to be able to raise the payout?

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Yes. I'll let David take that.

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Colin, we certainly recognize that changing the dividend is somewhat of a permanent change. And so we want to be pretty diligent and thoughtful when considering any dividend rate increase. As you know, we're comfortably funding our dividend right now with 2017 payout of 68%, based on CAD per share, and 75% payout if you factor in the additional real estate development investments. However, we also recognize that much of our growth in cash flow over the last few years has come from segments with a more with a higher degree of cash flow volatility, namely, New Zealand, Pacific Northwest and Real Estate. So our board evaluates the dividend level every year. We take into account our other capital allocation priorities as we do so. And keep in mind that as we put as we've described, we really like to remain nimble with respect to our capital allocation options with an eye towards always maximizing the long-term value per share. And over the past few years, we've deployed capital across a pretty broad expanse of those capital allocation alternatives, from acquisitions to share buybacks, always maintaining that nimble approach. So our board will be taking into account both the relative volatility of the sources of our cash flow as well as the relative attractiveness of various capital allocation alternatives when we're thinking about this going forward.

Collin Philip Mings - *Raymond James & Associates, Inc., Research Division - Analyst*

Okay. And then, maybe just on that point, as far as being nimble from a capital allocation standpoint. Just curious, particularly given some of the comments about there still being a pipeline of deal opportunities. Would an ATM program, like we see in other REITs, make sense for you guys? I don't think any other timber REITs have put one in place before. But would that be a tool that you're about to put into your toolbox?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

I mean, I think we're always looking at the full range of options within the ability to raise capital, and some of that's going to be a function of the uses of that capital as well as the attractiveness of transaction. I think an ATM is perhaps not as applicable to larger transactions. And we right now have a pretty decent cash balance that allows us to really pursue the bolt-on transactions without that.

Operator

Our next question comes from John Babcock with Bank of America.

John Plimpton Babcock - *BofA Merrill Lynch, Research Division - Associate*

I just want to touch back on the Southern Timber segment here for a second. Just you mentioned that pricing has been relatively flat, maybe up a little bit and also that the coastal Atlantic markets generally can tend to have a bit more tension as demand grows, and I was wondering if you could talk about the pricing trends that you've seen both in fourth quarter but also in the full year of 2017 there?

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Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

Sure. This is Doug. I'll talk about that. Yes, as we mentioned, geographic mix is going to be the biggest thing we see, and along the Atlantic coast, as Dave mentioned, through the years we saw some increases in lumber pricing as well as increasing in exports. We started to see some more tension in this market and some price traction on our sawlogs and our chipping saws. So that was real favorable. As we move further over towards the Gulf states, it was definitely lagging, and we didn't see that same amount of tension. So there's definitely a difference that we've seen across there. And as we have the shift next year in our harvest, that's one of the reasons we're talking about that, more volume shifting over to the gulf than we expect to be. Comparable, flat to 2017. But in reality, we'll have certain markets that we experience some price increases, particularly on those, the sawlogs, I believe.

John Plimpton Babcock - *BofA Merrill Lynch, Research Division - Associate*

Okay. And then just to, also, clarifying some of the comments earlier with rise of the Pacific Northwest. I was wondering how long you ultimately expect it to take for supply to catch up with demand in that region? And on top of that, how are you how you are ultimately thinking about the timing of recapture of the deferred harvest up there?

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

Yes. Let me go and get it first?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

Yes.

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

In the Pacific Northwest, what we've seen is that supply is starting to catch up with demand. I wouldn't say there it's equal yet, but log we are just trying to build some inventory. So we've seen that. So we've captured approximately 38,000 tons of that 50,000 tons in stumpage sales in the first quarter. So we've gone ahead and locked in quite a bit of that volume right upfront, out the gate. And we don't see that supply is going to from what we can see, it's not going to exceed demand, but we do see it getting closer than it was back when we hit the fire strips and other things were happening. So we've gone ahead and locked in that volume in the first quarter.

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

And recognize too that Northwest some of that Northwest export volume really can flow either to export markets in China, or into the domestic market in. So that interplay between those 2 will have a big bearing on the demand side of the equation.

John Plimpton Babcock - *BofA Merrill Lynch, Research Division - Associate*

Okay. And then, just on this topic, we've heard from a number of people throughout earnings, particularly in the Pacific Northwest, the transportation has been an issue. What impact, if any, has that had on your business and the kind of the demand that you're seeing?

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

Yes. It's a common theme that's out there. Whether it'd be the South of Northwest. That's more exposed to the Northwest I believe. Trucking has definitely been a limiting factor in some cases. We, as Dave mentioned, there are things we mentioned before we've in New Zealand, we've done

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long-term contracts. We've also done the same thing in the Northwest in cases. And so we haven't experienced any slowdown in ability to move logs to those customers or anything like that. But we do see price pressure as folks are competing for those drivers.

John Plimpton Babcock - *BofA Merrill Lynch, Research Division - Associate*

I got it. And then the last question before I turn it over. Just on the New Zealand guidance there. Looks like it's down a bit from 2017. What are you assuming in that guidance? And is there any sort of conservatism based in there? Or we really just kind of expecting some sort of volatility in that market to have an impact on results?

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

John, the primary driver of that is, we had the $24 million land sale in the second quarter of 2017 that we're not assuming in the next year. So we actually look at it excluding the impact of the transaction, it's actually forecasted to go up.

Operator

Our next question comes from Steven Chercover with Davidson.

Steven Pierre Chercover - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

So I too had a question on New Zealand. Only a couple of years ago, the guidance for the region was less than $30 million at the high end. And now the midpoint is triple that. So is that a function of increasing consolidation as you've increased your stake? Or has profitability changed that much?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

I think it's been a number of things, Steve. There has been modest increases in the footprint, but I'd say it's more driven by a combination of strong markets and favorable shipping logistics costs. You had a period where we had an abundance of vessels that service the log trade combined with low oil prices that translated into, in some of these periods, record low shipping rates at a time when you had very strong demand across the spectrum. We saw as well increasing substitution within China. Particularly on the plywood side, where we saw more radiata flowing into plywood, so that today, roughly 30% of radiata goes into plywood. We also saw the ban on the harvest of native forests in China due to overharvesting over a period of time. So that translated into a restriction on domestic supply at the same time that you had a strong growth in demand. And so the China market for logs has grown while the domestic supply has shrunk. And New Zealand has just been very well situated to compete in that market, both in terms of where those logs compete, both geographically and productwise, and then to combine that with very favorable shipping rates. So across that spectrum I'd say it's a much heavier mix from a margin standpoint.

Steven Pierre Chercover - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Can you even envision a scenario where we would go back towards that $30 million or lower run rate?

David L. Nunes - *Rayonier Inc. - CEO, President and Director*

It's hard to say with any certainly, but we certainly feel good about the trajectory of that market, and we certainly feel good about the level of consumption in China. Look, the reality is, China is massively net short on wood fiber, and we don't see that dynamic changing any time soon. I mean, Economic data shows that the per capita consumption of wood goes up as economies develop. China has a huge population, and they don't have the domestic fiber source to supply that need. And so we think the fundamentals are there to sustain a pretty good run in New Zealand.

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Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

You also, Steve, had pricing tends to be set on the margin, and you had a strong demand increases coming out of India during that period of time to where today India is pushing price instead of trailing. And so you've just had all of these factors kind of lineup at the same time.

Steven Pierre Chercover - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Yes, it looks great. It's hard to envision a scenario where China really goes back.

Operator

Our next question comes from Charan Sanghera with RBC Capital Markets.

Charan Sanghera - *RBC Capital Markets, LLC, Research Division - Senior Associate*

Two question on Southern harvest levels. I see you're at about 5.8 to 6 million tons for 2018. Any color on where you see this trending in 5 years or so? And also on the sawlog mix. It improved, particularly over last year. I think, might have probably due to acquisitions. But what's the trajectory for the mix shift? Like do we see 50% in the coming years or given relative pulpwood versus sawlog pricing? And does this stay lower, like i.e., like 40%?

Douglas M. Long - *Rayonier Inc. - SVP of U.S. Operations*

This is Doug. I'll start with that. The stable harvest that we publish is based on our own biological potential of our assets, and our annual harvest volumes are guided by this number, but we also take in account a bottom up approach from our timber marketing teams in the field to provide information on the kind of demand and what level of supply they believe will make an impact on our market prices. So as you can see that bottom up approach kind of going this year as, as you're able to get some, a little bit less than our biological calculation. And if we see a spot opportunity to capture market prices that exceed our expectations for the future, we have the flexibility to do some additional harvest. Going forward, we are tracking at least 2 billion ton onboard feed of sawmill capacity coming online in Rayonier's regions over the next few years. And if we think about patience, maybe warranted, but as we do go forward over the next couple of years, you mentioned, I we will see ourselves with the acquisitions we made, the project Tim really talked about, that's an increase we're seeing this year going forward that, we'll be in that more towards that sustainable harvest, I believe, due to demand that we have explained out there in next couple of years. With respect to the grade, we're also seeing that shift, and it will get go closer to the 50% that you mentioned over the next couple of years and continue to move on as we get into our standard of how we've done things over the last few years.

Operator

Our final question will come from Collin Mings with Raymond James.

Collin Philip Mings - *Raymond James & Associates, Inc., Research Division - Analyst*

Just 2 quick follow-ups for me. And you touched on this a little bit, but as far as some of the cost pressures you're seeing, just how successful are you able, as far as pushing that along to our customers? I mean, particularly in the U.S. South, just given the market, there isn't as tight as it is for logs as in the Pacific Northwest. To what extent are you able to put push along some of those incremental cost to customers on the actual delivered log sale?

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Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Yes, Collin, I would say that, so far we've been fairly successful with that. Realizing there's a lot more margin in the Southern Yellow Pine then there is out in the Pacific Northwest. So right now, we do see those pressures, but we've been effective at working through that at this point in time. There's just that much more margin that those sawmills have.

Collin Philip Mings - *Raymond James & Associates, Inc., Research Division - Analyst*

Okay. And then as far as New Zealand, just going back to the prior question, it looks like it's a you've touched on the inverse of this. But as far as in New Zealand, it does look like the harvest guidance for '18 is slightly above that sustainable yield range that was provided in November or December Investor Day slide deck. Is that just being opportunistic in terms of the market? Or anything else that we should be mindful of?

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Yes, Collin. It's really a function number of factors. I mean, you know what, I think we're the only company that discloses those long-term sustainable yields within each of our segments. But at a very basic level, sustainable yield, it's designed to reflect the volume of timber that we could theoretically harvest into perpetuity. It's really a concept of cutting growth, like Doug mentioned. That said, our actual yield in any given period is never going to be precisely in line with that sustainable yield, and really for a few reasons: first, you're invariably going to have some H-class variation in your portfolio. So the volume of the trees you got reaching economic maturity at any given year is going to be vary to some degree.

Second point I'd make is that, due to the improvements in silviculture and genetics, harvest models tend to be upwards sloping. So the stems that we're projected to cut 10, 20 years out are generally more productive than the stems that we're harvesting today. So as you might expect, if you looked at a 20-year or 50-year average of your harvest based on those model harvest flows, it's generally going to be higher than the volume that you're able to sustainably cut today. Last point I'd make is that portfolio changes are also going to impact that, that sustainable yield. So New Zealand is really a combination of all of those factors. We generally update our sustainable yield annually with the publication of our 10-K, and we do expect that, that sustainable yield in New Zealand will increase probably in the range of 5%, 10% based on a number of those factors that we just talked to. So and that's also reflective of some of the acquisitions that we made in 2017. So stay tuned. I would say that the projection for 2018 is generally in line with, maybe, modestly above kind of where that updated sustainable yield will be, and that's really just a reflection of both age class as well as trying to capture strong markets.

Operator

And with that, we'll conclude the question-and-answer session.

Mark D. McHugh - *Rayonier Inc. - CFO and SVP*

Well, thank you. This is Mark McHugh. I'd like to thank everybody for joining us. And please contact me with any follow-up questions.

Operator

Once again, with that we'll conclude today's conference. Thank you for your participation. You may disconnect your lines at this time.

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