



Trident Holdings LLC Proposed Land Exchange:

Economic Benefits to Idaho Endowment Beneficiaries

Analysis
conducted and
prepared by:



Overview

Trident Holdings LLC (Trident) of Boise, Idaho proposes to work with the Idaho Department of Lands (IDL) to develop a land and timber asset exchange of financially underperforming Idaho endowment lands in the Payette Lake area. The proposed exchange involves Trident acquiring designated “timberlands” from IDL endowment lands and a small number of unleased residential lots in Valley County, Idaho. These lands will be concurrently exchanged by IDL for privately-owned commercial timberlands in North Idaho that exceed IDL’s return threshold of 3.5%. These North Idaho timberlands will become new endowment timberlands.

Summary of Findings

- Research indicates the specific “economically impaired” lands subject to this exchange (~28,000 acres in Valley County) are significantly underperforming the State’s desired long-term return of 3.5%, contrary to the Idaho Constitution and Land Board Policy. Rather, these lands are a **major cost center to the endowment, losing an estimated \$276,000 annually, or negative \$7.9 million of real present value**. Positive returns from profitable endowment lands elsewhere are subsidizing these costs.
- The proposed exchange is estimated to generate more than **\$2.9 million** per annum of net revenues, returns and cost savings. This annual benefit, which existing assets cannot provide, **represents an additional \$84.7 million of real net present value to beneficiaries, notably Idaho schools and universities**. This total includes an incremental, accretive **\$19.6 million** value from non-exchange portfolio reallocations to meet Callan targets. Put simply, because the exchange provides the endowment with profitable lands for minimal cost, less Land Bank funds need to go toward timberland purchases to achieve target allocations, and more funds get invested in higher-returning, non-timber instruments like equities.
- Acquiring North Idaho timberlands near mid-rotation will **increase timber revenues from existing endowment forests for several decades** (estimated at \$14.2 million of present value, or over \$498,000 annually). IDL’s policy manages endowment timberlands to a non-declining statewide timber harvest, so buying younger mid-rotation trees enables the State to harvest more of its existing, older portfolio now.
- The proposed exchange will **improve physical and legal accessibility to existing North Idaho endowment lands**. Opening this access makes it possible to harvest endowment lands that are currently encircled, unlocking existing portfolio value (conservatively estimated at \$322,000 of present value).
- Obtaining income-earning timberlands from this exchange **reduces reliance on the Earnings Reserve**.
- IDL’s **potential alternatives do not offer comparable returns**. Neither a campaign to auction various smaller high-value parcels piecemeal nor a strategy of using only Land Bank funds to buy North Idaho timberlands outright (while retaining this cost center) would replicate the proposed exchange’s return.
- Trident appears **deeply committed to working with all parties involved, particularly local governments in Valley County and McCall**, to fulfill community requests for conservation and public access, and intends to bring additional employment and economic development to the region during a petax-based period of forecasted economic hardship. Trident also developed a potential long-term escrow fund structure to address tax-based concerns of Northern Idaho counties.

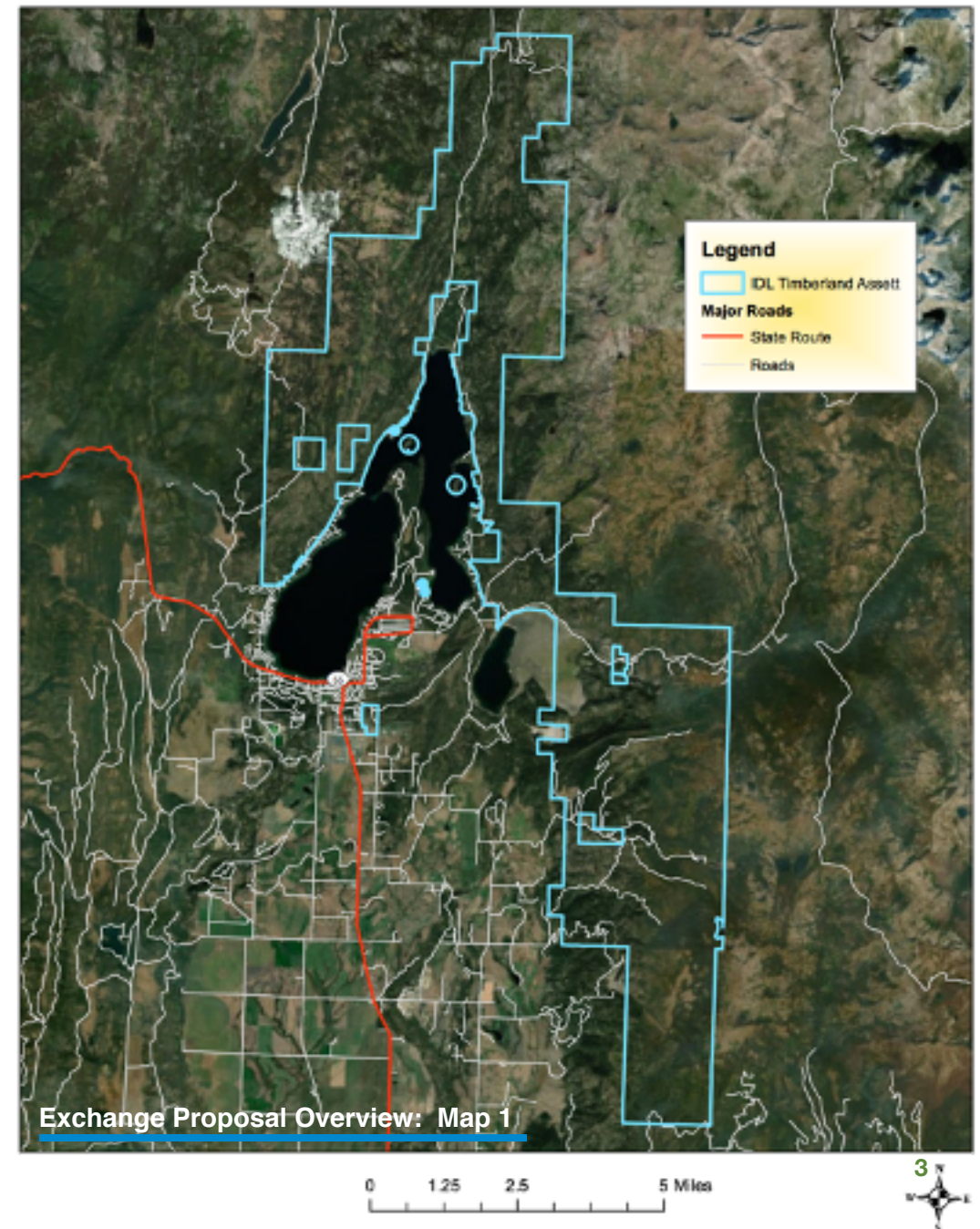
RESEARCH FOCUS

Smart Forest Solutions® was asked to perform an economic analysis of the proposed Trident Holdings LLC land asset exchange under the Idaho Constitution, the State Board of Land Commissioner's (Land Board) Statement of Investment Policy - Idaho Land Grant Endowments (SIP), and recent subcommittee findings and recommendations.

Asset Exchange Proposal

Through concurrent three-party agreements, this proposal exchanges economically constrained forested and a small number of unimproved and unleased lake lot land assets of several Idaho endowment beneficiaries in the Payette Lakes region. These would be exchanged for North Idaho working forests adjacent or in proximity to endowment forests within strong and growing timber market regions. This exchange explicitly supports the July 2018 Statement of Investment Policy (SIP).

The exchange will follow IDL-defined exchange procedures. Following IDL and the Land Board approval in concept of such an exchange, Trident Holdings and IDL staff will cooperatively identify endowment lands within the Payette and Little Payette regions best suited for eventual exchange. Upon completion of this joint planning initiative, Trident Holdings will also secure options to acquire suitable working forests for each endowment beneficiary from private forest owners adjacent or in proximity to endowment properties in North Idaho.

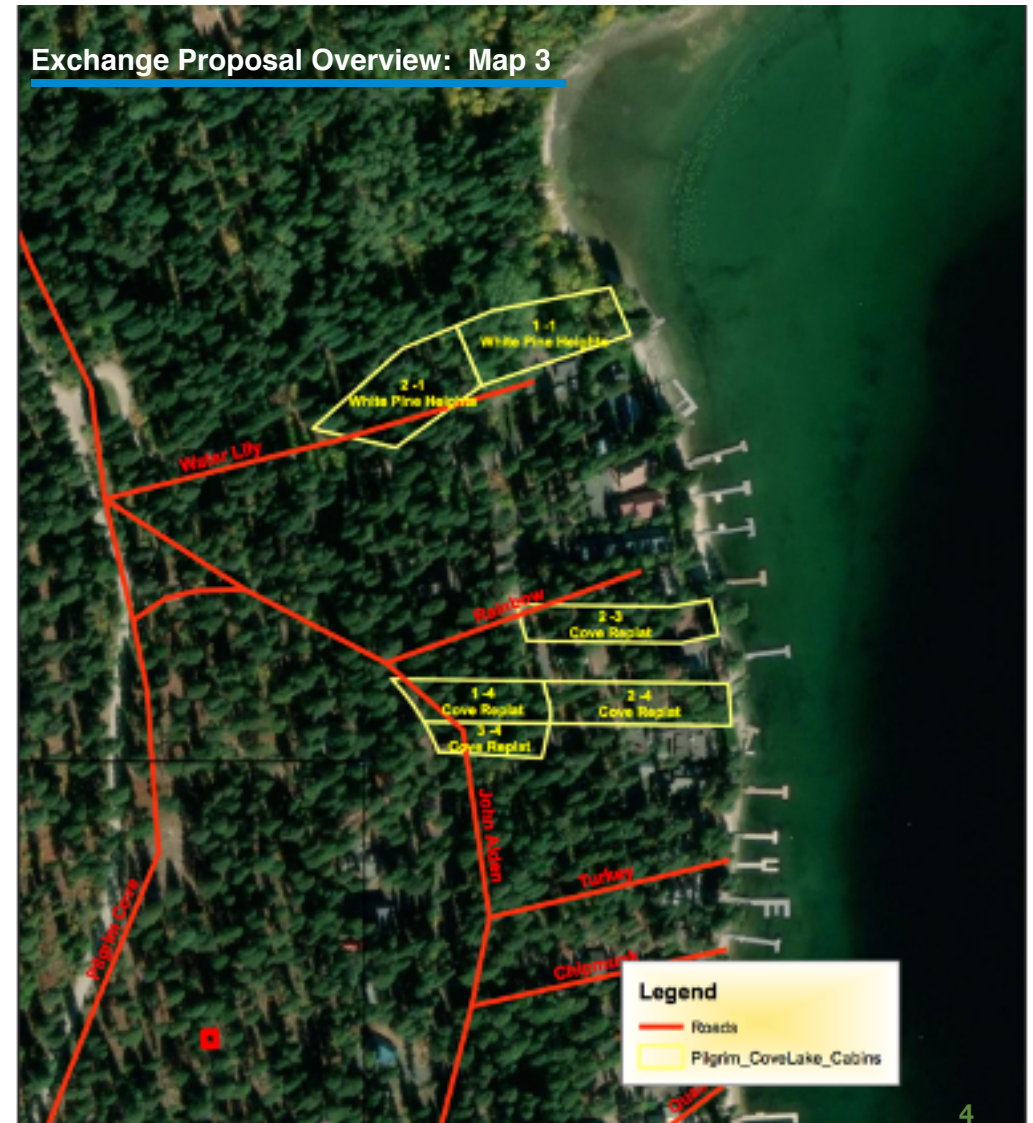


Exchange Proposal Overview Maps

Exchange Proposal Overview: Map 2



Exchange Proposal Overview: Map 3



Exchange Proposal Alignment to Policy and Objectives

The proposed exchange explicitly supports the *Idaho State Board of Land Commissioners Statement of Investment Policy* and the *Idaho Department of Lands Forest Asset Management Plan Goals and Objectives*:

As outlined in the July 17, 2018 SIP (p. 2),

“Article IX, Section 8 of the Idaho Constitution includes the following restrictions regarding the sale of lands:

- All land must be disposed of via public auction
- A maximum of 100 sections (64,000 acres) of state lands may be sold in any year
- A maximum of 320 acres may be sold to any one individual, company, or corporation
- No state lands may be sold for less than the appraised price
- Granted or acquired lands may be exchanged on an equal value basis with other lands subject to certain restrictions
- Forest and certain other land may not be sold per Idaho Code § 58-133, which states, “All state-owned lands classified as chiefly valuable for forestry, reforestation, recreation, and watershed protection are reserved from sale and set aside as state forests.”

The SIP also defines the Board’s asset allocation objectives, including those for increasing timberland assets (pgs. 5-6 of SIP replicated here).

Exhibit 1: Strategic Asset Allocation

Asset Class	Target Asset Allocation	Range	Actual Allocation June 30, 2017	Expected 10 Year Compounded Return ^{1,2}	Implied Real Net Return ³
Financial Assets	58%	50-65%	59.2%	6.3%	4.05%
IDL Timberland	39%	30-50%	33.2%	5.70%	3.45%
IDL Grazing Land	2%	0-5%	1.7%	3.00%	0.75%
Cash Equivalents –Land Bank	1%	0-5%	2.1%	2.00%	-0.25%
Residential Real Estate	0%	N/A	2.6%	N/A	
Idaho Commercial Real Estate	0%	N/A	0.5%	N/A	
Other Land	N/A	N/A	0.7%	N/A	
Total	100%			6.69%	4.44%
Expected Risk (Standard Deviation)				9.28%	
Inflation Assumption				2.25%	

Exchange Proposal Alignment to Policy and Objectives *(continued)*

The policy further defines land asset objectives explicitly, including the role of such assets in reducing overall volatility of endowment investment revenue and therefore the level of the *Endowment Earnings Reserve*, as follows (text selected from SIP p. 13-16):

“VII. Asset Class Policies for Land Assets

A. Investment Objective for the Land Assets

The primary objective for the Land Assets is the generation of maximum long-term return at a prudent level of risk using traditional land grant asset types. The Land Assets diversify the Financial Assets given the low correlations of timberland and rangeland to public capital markets. The Land Assets also lower the volatility of the total investment portfolio considering timberland and rangeland returns have historically exhibited lower volatility than equity asset classes. During periods of negative financial returns, Land Assets can provide a positive revenue stream to help maintain Earnings Reserves and stable Endowment distributions.

Investment objectives are long-term return objectives. The investment objective for the land portfolio recognizes that timberland is a primary driver of the overall return for land and that income from timberland and, to a lesser degree, all other lands are the primary generator of investment returns. The individual investment objectives for timberland, rangeland, and farmland reflect the long-term investment characteristics (return, correlation, and volatility) compared to other asset classes. Investment objectives also consider the existing base of land holdings along with management constraints, notably sales restrictions, acreage limitations, and the rent-setting and leasing processes. The return objectives should not be viewed in isolation but in relationship to one another.

The Land Assets are managed to achieve a real net return target of at least 3% over a long-term holding period (Land Assets Return Objective). The Land Assets Return Objective includes both income and appreciation, is net of all asset level expenses and fees, net of internal management costs (e.g., the cost of IDL management), net of all fees and costs of program management (e.g., legal and audit), and net of inflation as measured by the Consumer Price Index. While the Land Assets Return Objective includes both income and appreciation, the return is expected to be generated primarily from income.

New timberland acquisitions shall be subject to a thorough due diligence process (by IDL or a land advisor, consistent with the established governance structure) to determine the following:

- If the expected financial return generated by income exceeds the minimum hurdle rate of 3.5% real net;*
- Whether the return profile is sufficient relative to the risk taken, including an analysis of the transaction in terms of long-term financial return and risk to the Endowment;*
- Whether the transaction would facilitate improved management or improve the overall Endowment land ownership pattern in the area;*
- The existence of any potential risks, including but not limited to environmental or title-related issues.*

Parcels posing any significant risk as described in the due diligence analysis and those not meeting the minimum hurdle rate shall be avoided. The presence of minerals including sand and gravel can enhance the net return from timberland. Land Bank funds used for acquisition can only be used on behalf of the endowment from which the funds originated. The minimum return requirement for new investments will be reviewed and updated as necessary based on the Strategic Reinvestment Plan.”

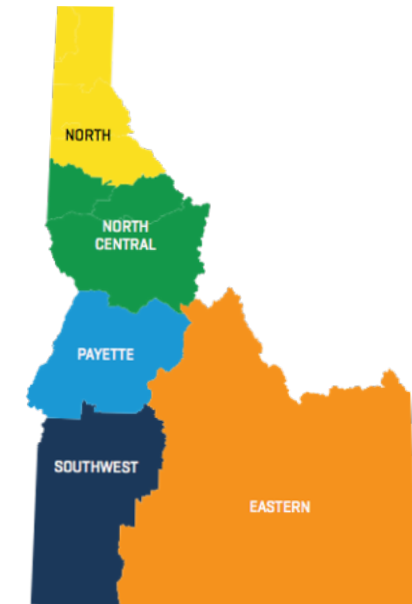
Payette Lakes Forest and Recreational Lake Lot Land Assets

IDL, on behalf of the endowment beneficiaries, manages approximately 105,022 acres of forested lands within the IDL Payette Lakes Supervisory Area.

Of the total, over 27,000 acres in the IDL Payette Lake's Supervisory Area are designated as “secondary forests.”⁽²⁾ This means these lands are economically impaired due to legal or physical access, low forest productivity, or Land Board aesthetic management policies limiting timber harvesting and road construction. **By statute the forested lands cannot be sold for other purposes and can only be exchanged for other forested lands.**⁽³⁾

By Land Board Policy and IDL forest management plans, endowment secondary forest lands within the Payette Lakes viewscape have undergone minimal harvesting for decades.⁽⁴⁾ These lands are therefore unable to partially or completely recoup IDL’s current annual \$23 per acre per year of timberland management expenses as of 2019.⁽⁵⁾ **Endowment income from profitable lands elsewhere in the state subsidize this loss. Eliminating this loss would therefore immediately increase average per acre returns across the entire land portfolio.**

Although endowment-appraised timberlands land values are not publicly available, land values of similar unimproved *but operable* forest tax appraised properties⁽⁶⁾ in Valley County, having lake views, range from \$98-\$2800 per acre depending on parcel acreage. These endowment secondary forest lands are therefore constrained to have a negative real return on assets until exchanged. **This economic loss is estimated to be -3.1% to -11.0% per annum depending on the land plus timber values assigned.**



⁽²⁾ IDL 2007 Forest Asset Management - MANAGEMENT GUIDELINES FOR ENDOWMENT TRUST FOREST LANDS WITHIN THE SECONDARY BASE

⁽³⁾ Idaho Code § 58-133 requires that all state-owned lands classified as chiefly valuable for forestry, re-forestation, recreation, and watershed protection be reserved from sale and set aside as state forests. Timberland can be exchanged but only for other timberland.

⁽⁴⁾ IDL 2014-2019 Timber Sale Annual Reports

⁽⁵⁾ IDL 2019 Annual Report

⁽⁶⁾ Valley County Idaho 2019 forested parcels greater than 40 acres, with lake views

2019 Payette Lakes Endowment Forest Lands Real Rates of Return

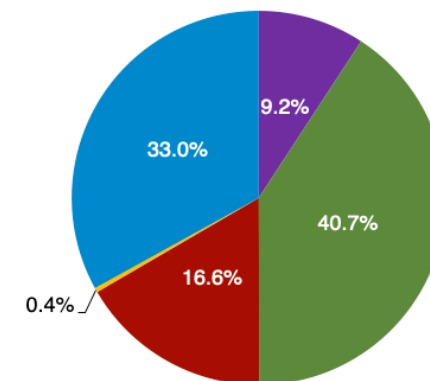
The potential exchange of these forested lands for forests capable of meeting the Land Board’s policy objective of 3.5% per annum real rate of return on timberland assets is viable and a financially sound opportunity. This represents a potential land exchange of up to 28,324 forested acres and 11.38 acres of platted lots.

Table 1: Estimated Financial Benefits Summary - Trident Holdings Proposed Exchange

	Trident Exchange Financial Benefits	Acres Contributing	Net Cash Income Per acre Per Annum	Annual Net Income	Net Present Value ⁽⁷⁾	Implied Net Cash Return on Exchange Assets
i	Reduce IDL Payette Lakes annual administration expenses <i>(low- or non-revenue lands)</i>	12,000 ⁽⁸⁾	\$23.00 (eliminated expenses)	\$276,000	\$7,885,714	0.79%
ii	Annuity Net Revenues <i>(Acquired North Idaho Timberlands)</i>	~20,508	\$59.50	\$1,220,230	\$34,863,705	3.50%
iii	Immediate allowable cut benefit <i>(existing endowment's mature primary forests)</i>	Existing endowment primary forest acres over 80 years old	n/a	\$498,333	\$14,238,095	1.43%
iv	Improve legal and physical access <i>(existing endowment lands)</i>	~1,280	\$8.80	\$11,270	\$322,000	0.03%
v	Portfolio reallocation to Callan-targeted non-timber assets <i>(see separate economic analysis)</i>	n/a	n/a	\$847,862	\$27,436,660	2.43%
Total				\$2,853,695	\$84,746,175	8.19%

Proposed Exchange's Annual \$3M Per Annum Income Represents \$77M in Portfolio Net Present Value

- Reduction in IDL Payette Lakes annual administration expenses (low- or non-revenue lands)
- Annuity Value of Net Revenues of Acquired North Idaho Timberlands (Acquired North Idaho Timberlands)
- Immediate allowable cut benefit (existing endowment's mature primary forests)
- Improved legal and physical access (existing endowment lands)
- Portfolio reallocation to Callan-targeted non-timber assets (see separate analysis)



⁽⁷⁾Discount Rate for benefits i-iv is the 3.5% real net return target for timberlands. Discount rate for benefit v is the endowment’s 3.09% real weighted average portfolio return excluding timberlands. Real forecasted rates of return were adjusted using Callan’s inflation projections of 2.25%.

⁽⁸⁾Eliminated expenses from this exchange are likely much greater than this, because this estimated reduction is based only on the 12,000 acres IDL identifies as secondary forest around Payette Lake, not the full administrative expense for the entire encumbered exchange area.

Northern Idaho Target Exchange Timberlands

Trident Holdings and IDL have identified, and are contracting with, a variety of large private forest owners known to be interested in divesting mid-rotation forest lands adjacent or in proximity to Endowment lands. These operable forest lands reside within six counties in western north central and northern Idaho. Market prices for fully accessible and operable mid-rotation (pole size) forests within these counties ranged from \$1500 to \$1800 per acre in 2019. The proposed land exchange would focus on acquiring highly productive mid-rotation forest lands adjacent or in proximity to existing endowment forests.

Potential real cash returns on these timberlands at current market prices range from 3.6-3.9% per annum, exceeding the Land Board's asset class target of 3.5% real cash returns.

SMART Forest Solutions' analysis of 2019 PNW trends in commercial timberlands cash returns on assets and Idaho market region's timber prices strongly supports the Land Board's investment policy to significantly increase the endowment's acreage of working forests.

Table 2: Northern Idaho Delivered Log Prices

TREESPECIES	2010 - 2019				AVERAGE
	MIN	MEDIAN	AVERAGE	MAX	2019
			\$/MBF		
Douglas fir/W Larch	277	386	365	402	385
Grand fir/W Hemlock	274	366	352	389	385
Lodgepole pine	275	370	352	388	367
Ponderosa pine	280	299	310	357	280
Spruce	279	366	353	400	348
Western white pine	286	332	326	337	337

Source: Northwest Management Inc.

Nominal prices were converted to constant 2019 dollars using the GDP implicit price deflator. Trend line was developed as base case projections and adjustments to the trends incorporated based on team analysis. The range of delivered log price compound annual growth rates for purposes of evaluating potential property returns ranged from 0.62% to 0.93% real, averaging 0.73% real.

Chart 1: Survey of Returns on Timberlands Investments in the Pacific Northwest



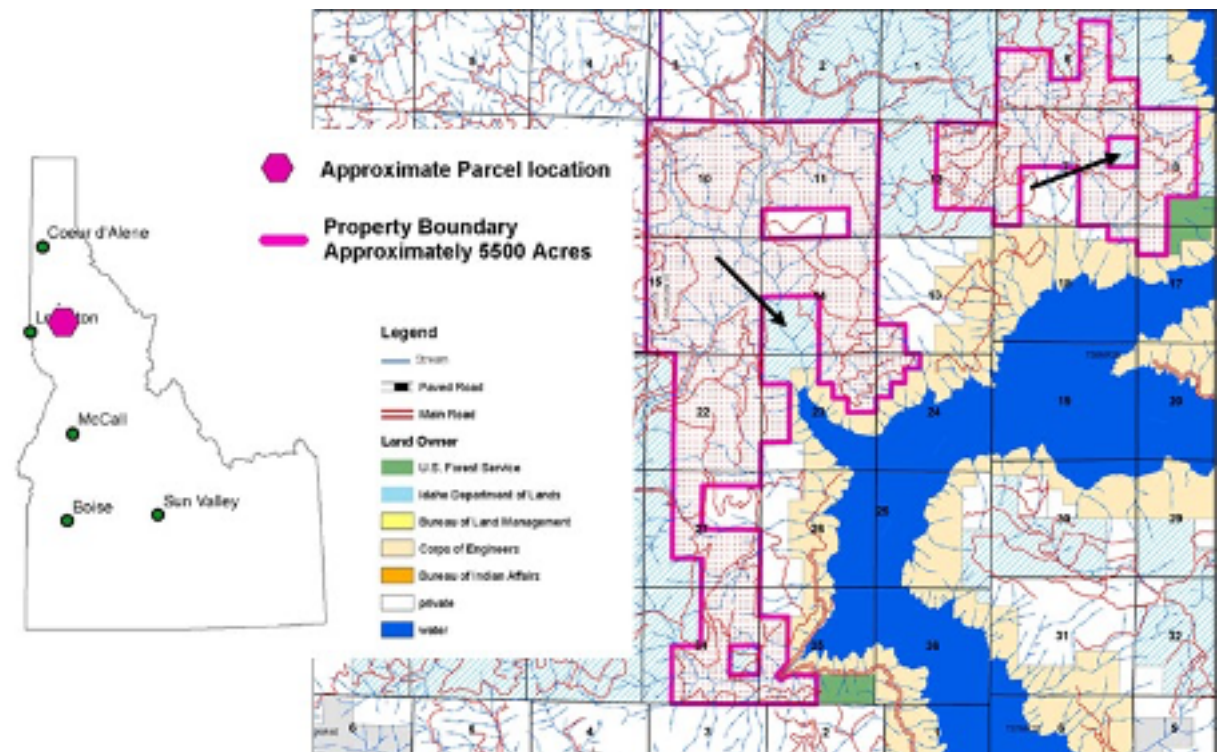
Additional, Significant Benefits of Endowment Timberlands Acquisition

Allowable Cut Benefit. IDL, in constructing its forest asset management plans, explicitly seeks to minimize the risk of declines in annual distributions to endowment beneficiaries and, by extension, minimize the total endowment earnings reserve. To achieve this, IDL Forest Asset Management Plans maintain a non-declining timber harvest policy. Given the age class structure of the endowment's forests, acquiring mid-rotation forests would facilitate near-term increases in timber harvests. IDL forest asset management planning during 2007-2008 identified improvements in real rates of return on investment of 0.15-0.47% through such acquisitions. Moreover, timber harvest net cash receipts of the acquiring supervisory areas would rise by +\$400,000 per annum for over 25 years (commencing immediately) by purchasing 6,000 acres of mid-rotation forests over five years.

Physical and Legal Access. In 2007 IDL identified approximately 245,000 acres of “secondary” endowment forests. Trident Holdings is unaware of the actual acreage of forested lands classified as secondary resulting from legal or physical access constraints. However, analysis of potential North Idaho exchange forest lands (examples highlighted by arrows in the map at right) highlights the opportunities to return even modest acreages of these forests to operable and accessible status.

While the benefit of improving access is very specific to potential exchange lands, the benefits are significant. Trident is ready to work with IDL staff to recruit such forests as part of a potential exchange.

Map 3: Examples of Potential IDL Exchange Properties



Financial Benefits Comparison

Comparison of Financial Benefits of Trident Holdings Proposed Land Exchange to Endowment Acquisition through Expenditure of Land Bank Funds

The endowment acquisition of timberlands via exchange or expenditure of Land Bank funds provides many of the same near and long-term financial benefits. However, the exchange of underperforming secondary forests has two very significant additional benefits, beyond what Land Bank purchases alone can provide:

- The proposed exchange represents a potential reduction of partial annual net losses on non or very low income-earning timberlands. In this case this is estimated to be greater than \$276,000 per annum.
- Per the Land Board's and IDL's utilizes Land Expectation Value methodology in deterring its annual timberlands asset value, any reduction in net losses improves both the remaining endowment timberlands values per acre and near- and long-term net cash returns on asset.

As of May 2020, the near-term price outlook for auctioning remaining unoccupied Payette Lake lots has diminished and can be expected to remain so for several years. In improving asset and product markets, public auctions can provide superior and transparent financial returns to the endowment beneficiaries.⁽⁹⁾ However, negotiated sales⁽¹⁰⁾ based on independent appraisals can provide significantly superior returns in declining commodity, art and real estate markets as a result of weighting in appraisals to historical income and comparable past sales. This strategy also avoids auctions with small numbers of participants taking bid price advantage of near-term uncertainty. It is clearly the fiduciary responsibility of IDL and Land Board to give consideration to this in their investment policies. The Trident Holdings LLC exchange opportunity for the proposed eleven lots would be based on appraisals of comparable recent past transactions.

⁽⁹⁾ Bulow, Harvard Business Review

⁽¹⁰⁾ The New Deal: Negotiauctions by Julia Hanna Harvard Business Review

Financial Benefits Comparison *(continued)*

There is one large additional (but difficult to quantify) source of value from Trident's proposed exchange that Land Bank purchases alone cannot produce. Per Callan's recommendations, IDL values timberland assets using "Land Expectation Value". This longstanding formula ($LEV = \text{Constant Real Annual Cash Flow} / \text{Real Annual Discount Rate}$) determines, in a standardized method, the long-term sustained value of the underlying land. This is not, in fact, an income-based asset valuation, which would equally take into account annual revenues and expenses, but then would also annually charge for the rotation or perpetuity land rent (at the discount rate) based on the underlying land value (from LEV or an appraisal).

This may at first seem complex, but it is important. It means that, in reality, the Endowment has three classes of timberland assets:

1. **Original Federal land grant acres**, for which the state of Idaho and its endowment invested zero dollars. Therefore, not charging annual land rent is correct, and a net present asset income based valuation is proper. LEV works fine for these lands
2. **Land Bank Fund cash acquired acres**. For these acres annual land rents should be expensed in their asset income valuation.
3. **Trident's Exchange Proposal**. The endowment also invests zero cash and therefore, as with the Federal land grant timberland acres, would properly have zero annual land rent charged in calculating a net present asset income based valuation.

These asset classes—with Land Bank purchases on one side, and Federal grants plus Trident's proposal on the other—will therefore have very different annual returns on investment, even for identical acres. IDL, when it values properties for cash acquisition, does take bare land value into account. However, it then ignores that value in its future LEV based asset reporting. This overstates true returns. By contrast, returns from Trident's proposed exchange avoid this pitfall.

Conclusion

It is the author's expert opinion that Trident Holding's proposed land exchange provides far superior financial returns to endowment beneficiaries over a Land Bank expenditure-only strategy and continued 2020-2021 auctions of unoccupied Payette Lake lots.

Trident Holdings' proposed lands exchange will significantly improve financial returns to endowment beneficiaries while also supporting the economic growth of Valley County, Idaho. SMART Forest Solutions, Trident Holdings and PRIMUS Policy Group look forward to working with the Idaho Department of Lands staff to implement this proposed exchange.

