



Timberland Investment Group Market Report

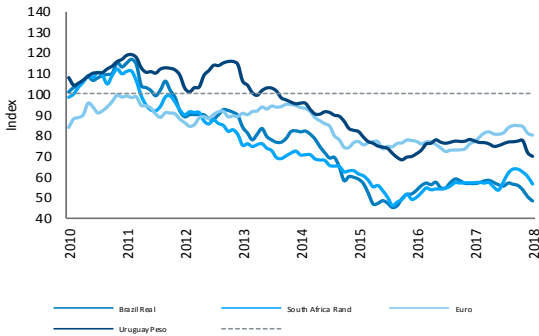
2nd Quarter 2018

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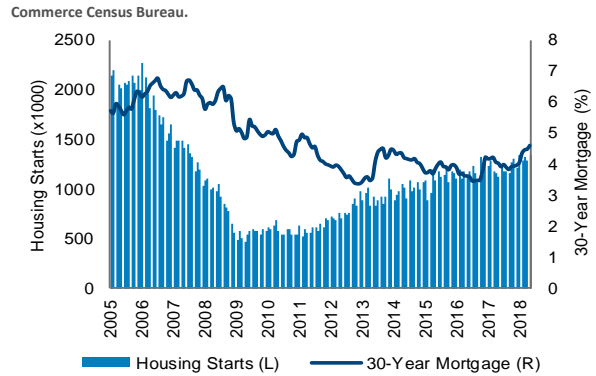
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Timberland Investment Dashboard

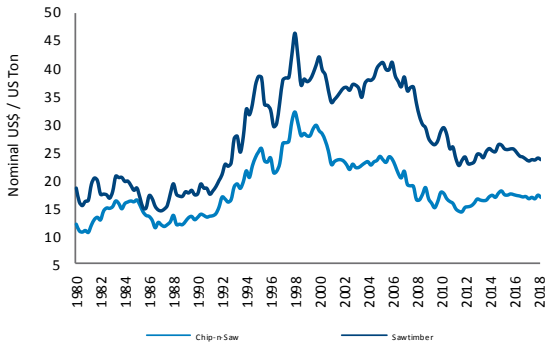
Indexed Exchange Rates of Selected Countries vs. the US Dollar (2009=100). Sources: Federal Reserve Bank; Bloomberg.



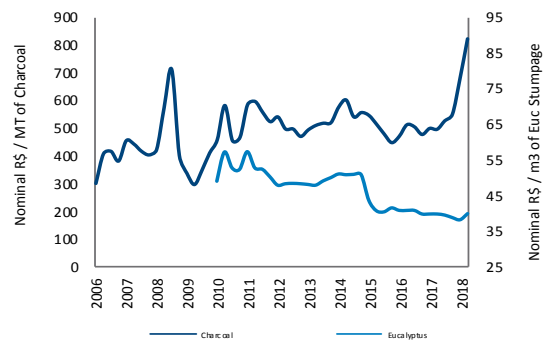
Annual US Housing Starts, Seasonally Adjusted Annual Rate, and 30-year Mortgage Rates. Sources: Federal Reserve Bank; US Dept. of Commerce Census Bureau.



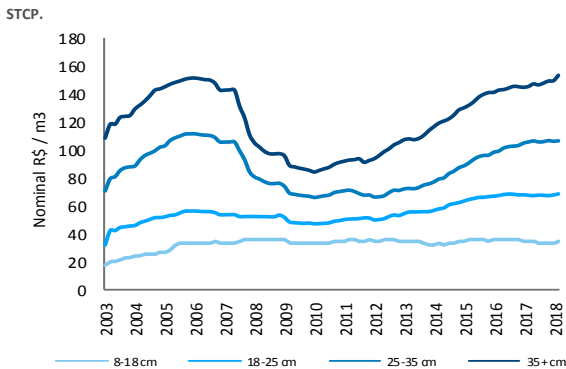
US Southwide Quarterly Pine Chip-n-Saw and Sawtimber Prices. Source: TimberMart-South.



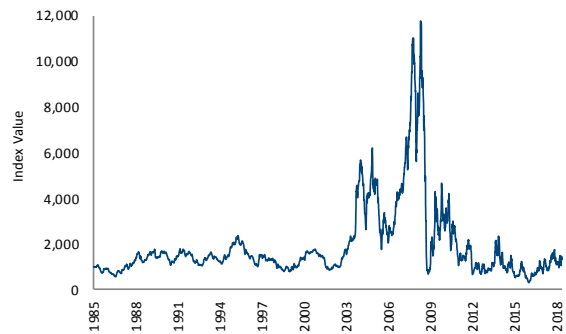
Quarterly Charcoal and Eucalyptus Stumpage Prices in Minas Gerais, Brazil. Sources: Associação Mineira de Silvicultura, Silviconsult.



Pine Sawtimber Stumpage Prices in Paraná State, Brazil. Source:



Baltic Dry Index. Source: Bloomberg.



Executive Summary

View from the Ground

- In the US South, prices were generally weaker as better weather led to increasing timber availability. However, sawtimber prices marginally increased in South Carolina, North Carolina, Georgia, Northeast Florida, and Alabama due to strong wood products demand.
- In the US Pacific Northwest, limited timber availability and contractor capacity, stable export demand, and accelerating domestic demand have resulted in tight timber markets and record timber prices.
- In Brazil, timber demand continues to improve in Minas Gerais given better pig iron demand and strong pulp demand. Elsewhere, timber demand has improved given better economic fundamentals while pulpwood remains oversupplied in certain regions.
- In Uruguay, pine sawlog prices were stable given steady export demand, particularly from China. Meanwhile, there is increased competition for eucalyptus pulpwood given the potential for a new UPM pulp mill.

Industrial & Capacity Update

- In the US, lumber producers continue to expand capacity through greenfield mills, capacity expansions at existing mills, and acquisitions. During the quarter, Roy O. Martin began production at its new Corrigan, TX OSB mill. Nine Dragons, China's largest paper and board producer, announced plans to buy Catalyst's paper mills in Rumford, ME and Biron, WI, while Green Bay Packaging announced plans to construct a new 685,000 ton recycled containerboard mill in Green Bay, WI.
- In Brazil, Duratex announced a joint venture with Lenzing to build a new dissolving wood pulp mill in the state of Minas Gerais. Royal Golden Eagle announced that it entered into an agreement with Lwart Group to acquire 100% of Lwarcel Celulose's assets in São Paulo. Brazil's anti-trust agency CADE approved Suzano's acquisition of Fibria.

United States

- The US economy expanded at an annual rate of 2.0% in Q1 (real GDP), unemployment slightly increased to 4.0% in June versus 3.8% in May, the Institute for Supply Management ("ISM") Purchasing Managers Index increased to 60.2% in June versus 58.7% in May, and May housing starts increased 5.0% over the prior month and 20.3% versus May 2017. The overall economic outlook remains positive.
- Southern pine sawtimber prices declined -1.3% for the quarter, but increased 1.0% year-over-year.
- Southern chip-n-saw prices declined -2.3% sequentially in Q2, but increased 1.4% year-over-year.
- Southern mixed hardwood sawtimber prices declined -1.2% for the quarter, but increased 4.1% year-over-year.
- In the US South, softwood pulpwood prices declined -2.8% quarter-over-quarter, but increased 0.8% year-over-year while hardwood pulpwood prices declined -0.4% quarter-over-quarter, but increased 18.8% year-over-year.

Latin America

- In Q1, Brazil's economy expanded with real GDP increasing 0.4% quarter-over-quarter versus an increase of 0.2% quarter-over-quarter in Q4.
- For the three months ended April, Brazilian softwood sawtimber prices were generally positive, depending on assortment, with veneer logs (large-diameter) experiencing more notable year-over-year gains.

- In Q2, Brazilian charcoal prices increased 65.7% year-over-year and have continued a strong upward trajectory into Q3. The price of eucalyptus used in charcoal production increased 0.3% year-over-year.
- Eucalyptus pulpwood prices in Brazil declined -0.4% for the three months ended April and -0.7% year-over-year.
- Uruguay's real GDP increased at an annualized rate of 2.2% in Q1 versus 2.0% growth in Q4.
- Eucalyptus pulpwood prices in Uruguay were flat quarter-over-quarter and year-over-year in Q2.
- Elsewhere in Latin America in Q1, Chile's real GDP increased 4.2% year-over-year, Argentina's real GDP increased 3.6% year-over-year, and Guatemala's real GDP increased 2.0% year-over-year.

Europe

- In Q1, euro zone real GDP increased 0.4% quarter-over-quarter versus 0.7% quarter-over-quarter growth in Q4.
- In Estonia, pine sawlog prices increased 19.9% year-over-year while birch sawlog prices increased 18.9% year-over-year. Estonian pine pulpwood prices increased 82.0% year-over-year while birch pulpwood prices increased 90.6% year-over-year.

South Africa

- South Africa's real GDP declined -2.2% quarter-over-quarter in Q1 versus growth of 3.1% quarter-over-quarter in Q4.
- In May, lumber prices increased 0.7% versus the prior three months and 1.0% from May 2017.
- Softwood log prices were positive. In Q1: A grade logs increased 4.7% for the quarter and 10.5% year-over-year, B grade logs increased 1.7% for the quarter and 7.0% year-over-year, C grade logs rose 2.0% for the quarter and 7.1% year-over-year, and D grade logs declined -1.0% for the quarter, but increased 3.5% year-over-year.

New Zealand / Australia

- In Q1, New Zealand's real GDP grew 0.5% quarter-over-quarter versus growth of 0.6% quarter-over-quarter in Q4.
- New Zealand A-grade export log prices increased in March given declining port inventories and steady demand in China, New Zealand's largest export market. Domestic log prices increased given steady demand for domestic lumber and limited log supplies in certain regions.
- In Q1, Australia's real GDP increased 1.0% quarter-over-quarter versus growth of 0.4% quarter-over-quarter in Q4.
- Australian softwood roundwood prices increased partly due to steady export demand from China while prices of hardwood logs also increased. Both softwood and hardwood chips moved higher.

Global Pulp & Paper Markets

- In Q2, bleached hardwood kraft pulp ("BHK") prices increased 3.5% versus Q1 and 33.4% year-over-year.
- Prices improved largely due to unexpected mill downtime and steady/improving demand.
- Bleached softwood kraft pulp ("BSK") prices increased 9.8% versus the prior quarter and 34.7% year-over-year.
- During the quarter, softwood pulp pricing increased given steady demand, maintenance downtime in North America which reduced supply, and as softwood producers looked to maintain a positive price spread with hardwood pulp.

*GDP is reported in real terms while timber pricing is reported in nominal terms

**For every country mentioned in this report, real GDP reflects 1Q2018; 2Q2018 real GDP will be released between late July 2018 and mid-October 2018

United States

In Q1, US real GDP expanded at an annual rate of 2.0% versus 2.9% in Q4 (Figure 1). The Q1 increase in real GDP reflected growth in nonresidential fixed investment, personal consumption, exports, federal government spending, and state and local government spending partly offset by negative contributions from private inventory investment and residential fixed investment. Imports also increased, which subtract from GDP. The unemployment rate slightly increased to 4.0% in June versus 3.8% in May while the change in total nonfarm payroll employment (seasonally adjusted) was 213,000 in June versus 244,000 in May. Meanwhile, the labor force participation rate slightly increased to 62.9% in June from 62.7% in May, continuing to trend along low levels (Figure 2).

Economic activity in the manufacturing sector continued to expand in June. The ISM, a bellwether of manufacturing activity, increased to 60.2% in June from 58.7% in May (Figure 3). The ISM is a diffusion index with values over 50% indicating growth and values below 50% indicating contraction.

Figure 1. Annualized Quarterly US Real GDP Growth (%).

Sources: US Dept. of Commerce, BEA.

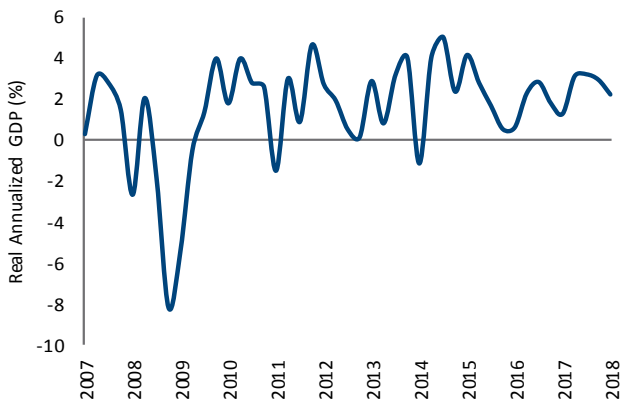


Figure 2. US Unemployment, and Labor Force Participation Rate.

Sources: Sources: US Dept. of Labor, BLS.

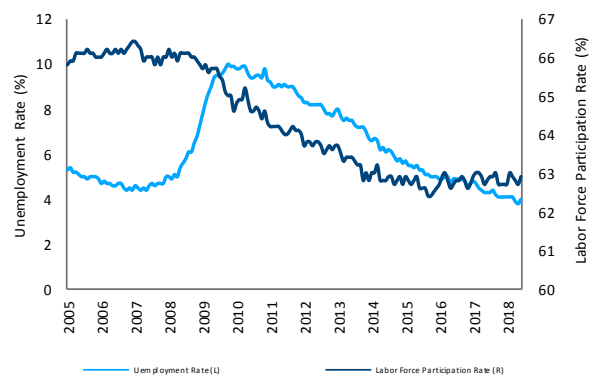
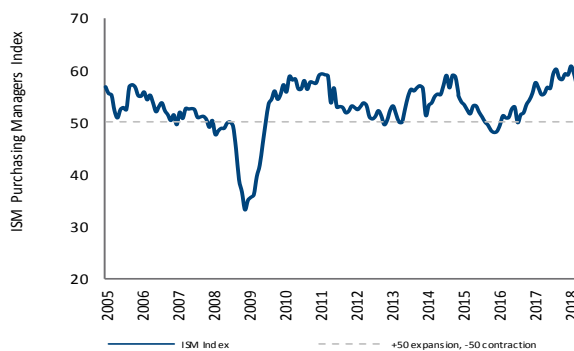


Figure 3. US ISM Purchasing Managers Index.

Source: Institute for Supply Management.



US housing

The US housing market continues to improve at a gradual pace. In May, housing starts were at a seasonally adjusted annual rate (“SAAR”) of 1.35 million units (Figure 4). This figure is up 5.0% versus April’s 1.286 million units (SAAR) and 20.3% versus May 2017’s 1.122 million starts (SAAR). The share of multifamily starts as a percentage of total starts increased to 30.7% versus 29.9% in April.

New single-family home sales increased 6.7% month-over-month in May (Figure 5). Existing home sales slightly declined -0.4% month-over-month in May (-3.0% year-over-year) to 5.43 million units (SAAR). Inventories of existing homes increased to 4.1 months in May versus 4.0 months in April, still a very low level of inventory by historical standards.

Figure 4. Annual US Housing Starts, Seasonally Adjusted Annual Rate and 30-year Mortgage Rates. Sources: Federal Reserve Bank of St. Louis,

US Dept. of Commerce Census Bureau.

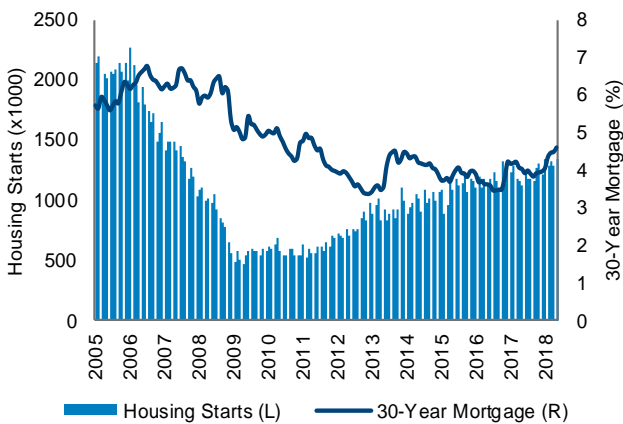
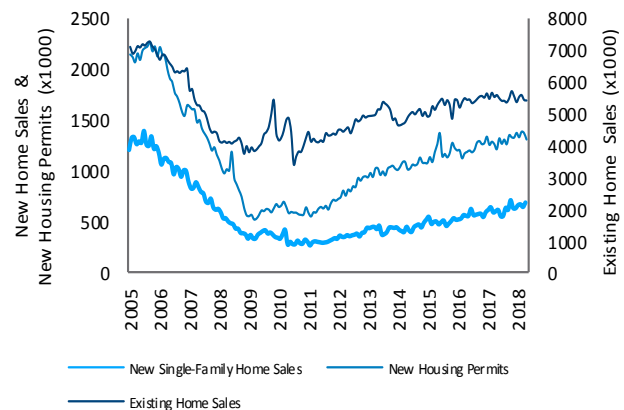


Figure 5. Monthly New Home Sales, New Building Permits, and Existing Home Sales, Seasonally Adjusted Annual Rates. Sources: US Dept. of Commerce Census Bureau, National Association of Realtors.

Bureau, National Association of Realtors.



In May, building permits declined -4.6% month-over-month. This decline was driven by an -8.8% month-over-month decline in multi-family permits and a -2.2% month-over-month decline in single-family permits.

US forest products and timber markets

Wood products markets experienced positive pricing momentum earlier in Q2 before prices began to soften later in the quarter. In aggregate, softwood lumber prices increased 11.7% quarter-over-quarter. This compares to a historical average sequential increase of 2.3% over the last decade (Figure 6). Through April & May, lumber prices increased due to strong demand, extended order files, lean inventories, and some logistical issues stemming from inclement weather. However, prices began to soften in June as buyers refrained from purchasing and mills looked to move product by offering discounts.

During Q2, structural panel pricing increased 8.9% quarter-over-quarter. This compares to a historical average sequential increase of 4.2% over the last decade (Figure 6). Similar to lumber, Oriented Strand Board (“OSB”) prices increased during April and May due to extended order files and limited supplies. However, OSB prices in most regions began to soften in early June due to slower sales and discounts offered to move inventory. By the end of Q2, Southeast 7/16” OSB prices had declined -9.4% to US\$ 415/msf versus US\$ 458/msf in late May. Meanwhile, Q2 plywood prices increased during April and May due to steady demand, but began to soften in June as order files declined and many buyers only purchased to fill immediate needs. By the end of Q2, Southern Plywood 15/32” 4-ply prices had declined -7.4% to US\$ 533/msf versus US\$ 575/msf in early June.

Figure 6. US Framing Lumber Index and Panel Composite Index.

Source: Random Lengths.

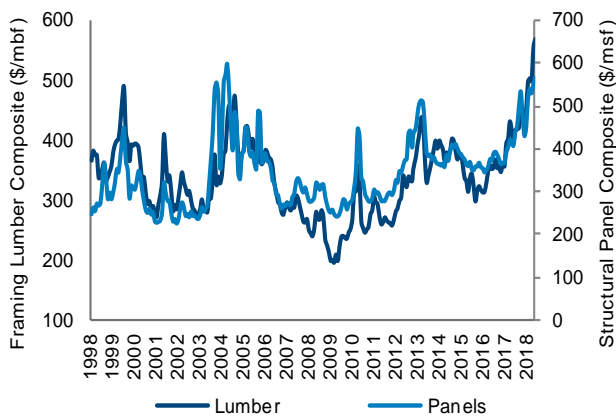
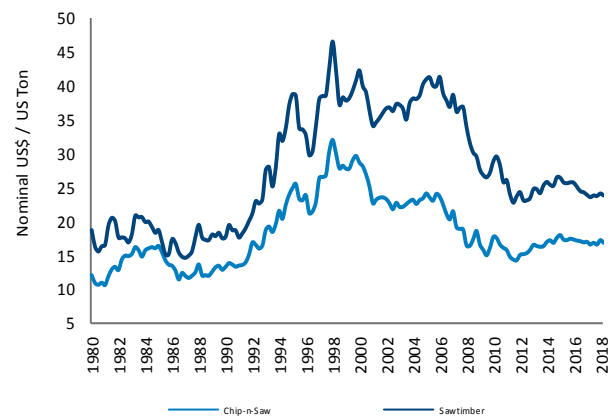


Figure 7. US Southwide Quarterly Pine Chip-n-Saw and Sawtimber Prices. Source: TimberMart-South.



Throughout the US South, pine sawtimber prices declined -1.3% in Q2, but increased 1.0% year-over-year according to TimberMart-South (Figure 7). Chip-n-saw prices declined -2.3% sequentially in Q2, but increased 1.4% year-over-year. Pine sawtimber and chip-n-saw prices averaged the highest in Florida and lowest in Tennessee.

Southern hardwood sawtimber prices were mixed during Q2. Region-wide, mixed hardwood sawtimber prices declined -1.2% for the quarter, but increased 4.1% year-over-year. Oak sawtimber prices increased a slight 0.2% quarter-over-quarter and 0.9% year-over-year (Figure 8).

In New York’s Adirondack region, northern red oak declined -2.3% quarter-over-quarter and -0.9% year-over-year. Hard maple declined -4.3% quarter-over-quarter and -4.8% year-over-year (Figure 9).

Figure 8. US Southwide Quarterly Mixed Hardwood and Mixed Oak Sawtimber Prices. Source: TimberMart-South.

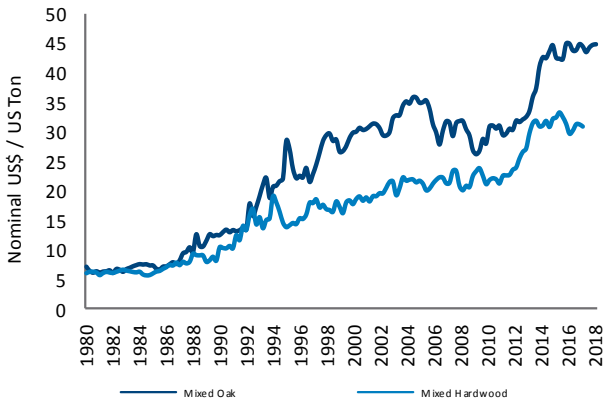
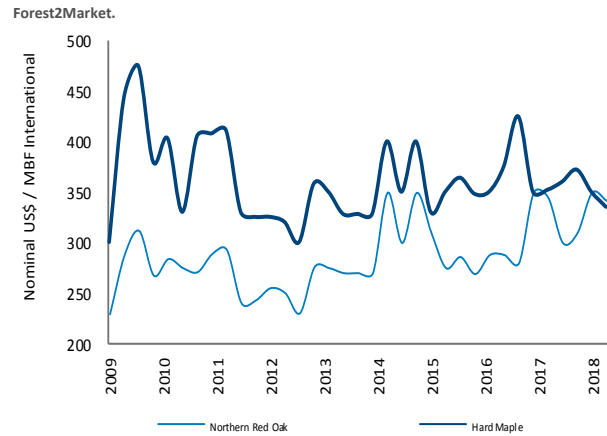


Figure 9. Quarterly Northern Red Oak and Hard Maple Sawtimber Prices in New York. Source: Forest2Market.



In Ohio, red oak declined -21.3% versus Q1, but increased 5.7% year-over-year. Hard maple increased 19.7% during the quarter and 32.3% year-over-year. White oak declined -20.3% quarter-over-quarter and -11.5% year-over-year (Figure 10).

In Wisconsin, northern red oak increased 6.3% quarter-over-quarter in Q2 and 9.0% year-over-year (Figure 11). Hard maple increased 5.6% quarter-over-quarter and 7.1% year-over-year. Yellow birch sawtimber was flat quarter-over-quarter and year-over-year.

Figure 10. Northern Red Oak, Hard Maple, and White Oak Sawtimber Prices in Ohio. Source: Forest2Market.

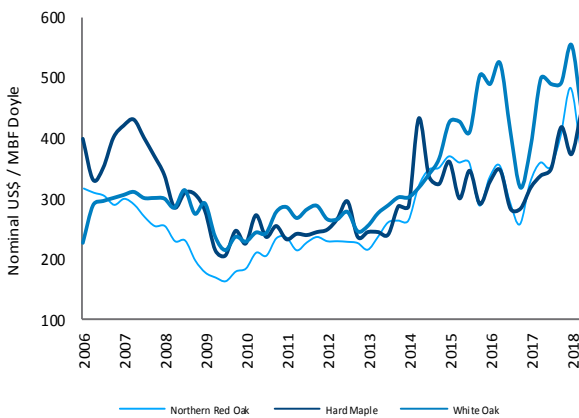
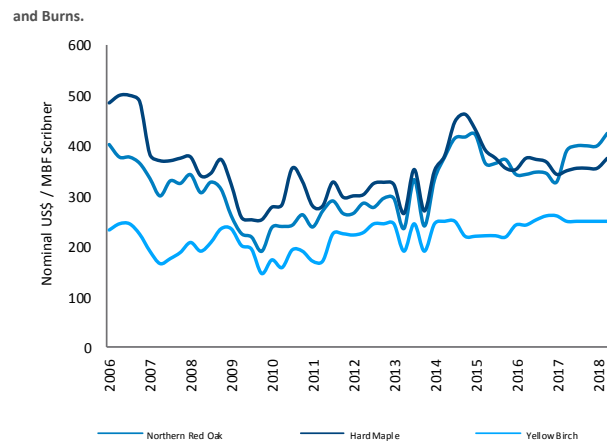


Figure 11. Northern Red Oak, Hard Maple, and Yellow Birch Sawtimber Prices in Wisconsin. Source: Steigerwaldt and Burns.



In the Pacific Northwest, softwood sawlog prices were generally better across all grades. While the price of Douglas-fir #2 modestly declined -1.0% sequentially, it increased 23.2% year-over-year (Figure 12). As of May 2018 (latest data available), Douglas-fir #2 is now 11.6% higher than its prior 2014 peak. The price of Whitewood #2 logs increased 0.7% for the quarter and 25.0% year-over-year. As of May 2018, Whitewood #2 is now 2.7% higher than its prior 2014 peak. In March 2018 (the latest available data), total softwood log exports to China increased 1.7% year-over-year to 84.75mmbf from 83.36mmbf in March 2017 and softwood log exports to Japan increased 0.4% year-over-year to 33.26mmbf from 33.14mmbf in March 2017.

In the US South, hardwood pulpwood prices declined -0.4% in Q2, but increased 18.8% year-over-year while pine pulpwood prices declined -2.8% quarter-over-quarter, but increased 0.8% year-over-year (Figure 13).

Figure 12. Monthly Columbia River #2 Douglas-fir and Mixed Whitewood Log Prices. Source: Log Lines.

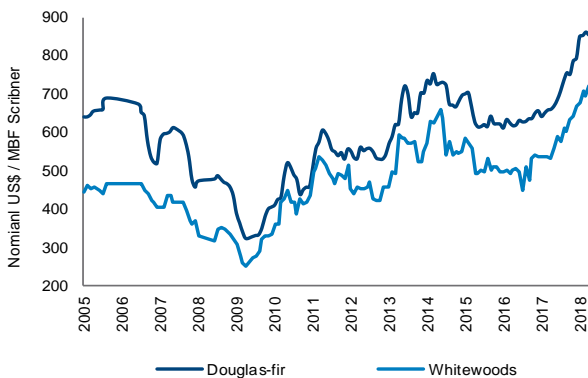
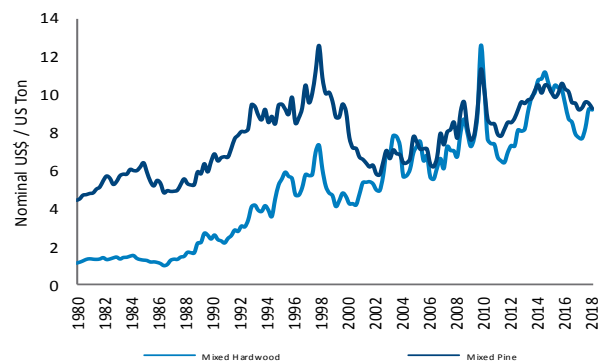


Figure 13. US Southwide Quarterly Mixed Hardwood and Mixed Pine Pulpwood Prices. Source: TimberMart-South.



Industrial & Capacity Update

During the quarter, Conifex agreed to acquire the Suwannee sawmill in Florida and the Caddo River sawmill in Arkansas with total capacity of 370mmbf from Blue Wolf Capital Partners for US\$ 200 million (~US\$ 540/mbf). Vicksburg Forest Products, whose parent company also owns Southeastern Timber Products, announced that it is reopening the former Anderson-Tully lumber mill (100mmbf) in Vicksburg, MS. The mill had been operating as a hardwood lumber mill, but will be upgraded to allow for the production of southern yellow pine lumber. Separately, Roy O. Martin began production at its new Corrigan, TX OSB mill.

In paper and board, DS Smith, one of the largest producers of corrugated packaging from the United Kingdom, announced its intention to acquire Corrugated Container Corporation, a corrugated packaging company in North America. In June, International Paper, a global producer of renewable fiber-based packaging, pulp and paper products, announced that it wouldn't make an offer for Smurfit Kappa given the lack of engagement by Smurfit Kappa's board of directors and management. In late June, Nine Dragons, China's largest paper and board producer, acquired Catalyst's paper mills in Rumford, ME (438,000 tons of coated paper; 114,000 of kraft pulp) and Biron, WI (335,000 tons of coated groundwood paper) for US\$ 175 million, making its first foray into the US markets. Green Bay Packaging also announced plans to construct a new 685,000 ton recycled containerboard mill in Green Bay, WI for US\$ 500 million with production

scheduled to begin in 2021 while Pratt Industries announced that it intends to spend US\$ 42 million to expand its box plant in Lehigh County, PA. Moreover, Sun Paper, which had originally intended to build a new fluff pulp mill in Arkadelphia, AR for US\$ 1.3 billion, now intends to build a new linerboard mill for US\$ 1.8 billion. Given the change in end-products, Sun Paper has had to reapply for new permits from the Arkansas Department of Environmental Quality and US Environmental Protection Agency.

View from the Ground

BTG Pactual Timberland Investment Group (“TIG”) regional foresters regularly report on conditions that impact wood pricing in their operating areas. In South Carolina, North Carolina, Georgia, Northeast Florida, and Alabama, wood products demand remains strong resulting in marginally better sawtimber prices. Land sales activity has also increased. That said, TIG’s foresters expressed concerns that the typical summer slowdown in timber sales could negatively impact pricing.

In East Texas, pulpwood remains oversupplied. Some of this excess may be absorbed by Roy O. Martin’s new OSB mill in Corrigan, Texas which is currently running at 40% of capacity and expected to reach full capacity by January 2019. Further, there are rumors that German Pellets is looking to restart its idled pellet plant in Woodville, TX which could consume around 1.0-1.2 million tons of pulpwood when fully restarted. That said, the site remains inactive. Similarly, the pine sawtimber market remains oversupplied with mills having ample inventories. However, the start-up of Angelina Forest Products’s new 220mmbf lumber mill in Q2 2019 could help to absorb some of that excess supply.

In Southwest Arkansas, pine pulpwood demand is stable as mills from Domtar and Huber Engineered Wood build inventories ahead of maintenance outages in September, which are expected to last 2-4 weeks. That said, prices are expected to come under pressure once downtime begins. Meanwhile, hardwood pulpwood pricing is positive given good demand and limited supplies. With respect to pine sawtimber, prices are under pressure given excess supply and the lack of a normal seasonal price increase due to inclement weather. During Q2, Southwest Arkansas received 40% of its annual rainfall in a 6-week period, yet sawtimber prices remained largely flat due to excess timber inventories.

In Virginia, pine pulpwood prices declined \$1-2/ton as WestRock leveraged its pending acquisition of KapStone to negotiate more favorable wood pricing. If the acquisition is approved, WestRock will control the four largest integrated board mills in Virginia.

In Ohio, demand for hardwood sawtimber remains strong given growing end-markets including whiskey barrels, railroad ties, flooring, and furniture, resulting in better timber pricing. Inclement weather due to summer rains has also helped push sawtimber pricing higher. Over the last few months, there has been increased speculation regarding Glatfelter’s strategy concerning its paper business including its Chillicothe mill as the company continues to expand into specialty businesses (e.g., Glatfelter is acquiring Georgia-Pacific’s European airlaid business) while minimizing its paper business.

In Appalachia, demand for quality hardwood sawtimber continues to be strong given growing domestic end-markets including railroad ties and good export demand.

In Central and Southern Alabama, mills have begun to put small quotas on loggers given the amount of available timber supply, which has increased as weather has improved. Georgia-Pacific's new mill in Talladega and the upcoming Rex Lumber greenfield mill in Pike County should be positive for sawtimber demand.

In Wisconsin, hardwood pulpwood prices declined \$2-3/ton given increasing timber availability from better weather and increasing haul rates.

In the Pacific Northwest, limited timber availability and contractor capacity, stable export demand, and accelerating domestic demand have resulted in tight timber markets and record timber prices. Timber sales continue to garner multiple bids. These favorable conditions are expected to persist for at least another 12 months.

Paper & forest products duties

In April, China's Ministry of Commerce announced that it will continue to impose anti-dumping duties on dissolving pulp imports from the US (and Canada and Brazil), following a re-investigation of a 2014 decision. The Ministry again adjudicated that the Chinese dissolving pulp industry has experienced material injury from those imports.

In May, the United States announced the imposition of tariffs on imports of certain steel and aluminum products from Canada. In response, the Canadian government imposed a 10% surtax on US goods including plywood, veneered panels, and paper & paperboard amongst other products.

In early July, the World Trade Organization ("WTO") announced that US countervailing duties against Canadian glossy paper imports violated international trade rules. Since 2015, the US has been imposing duties ranging from 17.87% to 20.18%. Specifically, the WTO panel objected to the way in which the US calculated its countervailing duties on Canadian exports of supercalendered paper. Following this announcement, the US Department of Commerce revoked the duties to their start date in August 2015, and agreed to repay the affected companies with interest.

Latin America

Brazilian economy

In Q1, Brazil’s economy expanded with real GDP increasing 0.4% quarter-over-quarter following a 0.2% quarter-over-quarter increase in Q4. Agricultural production increased 1.4% quarter-over-quarter while both industrial activity and service activity slightly increased 0.1% quarter-over-quarter. Investment increased 0.6% quarter-over-quarter following a 2.1% quarter-over-quarter increase in Q4. BTG Pactual’s Brazilian Economics team currently expects 2018 real GDP of 1.4% and 2019 real GDP of 2.0%.

As part of this modest improvement, household spending increased 0.5% quarter-over-quarter in Q1 versus 0.1% quarter-over-quarter growth in Q4. Unemployment slightly declined to 12.7% in May from 12.9% in April. Moreover, industrial production declined -6.6% year-over-year in May due to the truckers’ strike (see below) after increasing 9.0% year-over-year in April.

During the quarter, inflation increased partly due to higher transport costs and agriculture prices related to food shortages from the truckers’ strike (see below). As a result, the Índice de Preços ao Consumidor Amplo or “IPCA” increased to 4.39% annualized in June from 2.86% annualized in May and 2.76% annualized in April (Figure 14). Real rates have also trended somewhat higher as evidenced by rising Treasury inflation-protected bond yields (Figure 15). In June, Brazil’s central bank held the Selic rate flat at 6.50% as it continues to evaluate economic conditions.

Meanwhile, exports increased 1.3% sequentially in Q1 following a decline of -0.8% quarter-over-quarter increase in Q4. Imports increased 2.5% sequentially after increasing 1.6% in Q4. Separately, in Q2, the real depreciated 10.8% sequentially (Figure 16) given concerns around economic growth and political uncertainty. Given increased currency volatility, the Brazilian Central Bank has increased its currency swap program.

Figure 14. Brazilian SELIC Rate and Annualized IPCA Index.

Source: Banco Central do Brasil, Brazilian Institute of Geography and Economics.

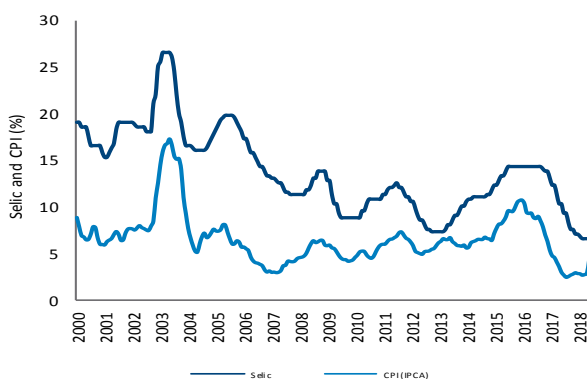


Figure 15. Brazilian Treasury Inflation Protected Bond Yield. Source: Brazil National Treasury.



Figure 16. US Dollar: Brazilian Real Daily Exchange Rates.

Source: Board of Governors of the US Federal Reserve System.



Political conditions in Brazil remain volatile. Brazil’s Supreme Court canceled former President Luiz Inacio Lula da Silva’s trial scheduled for late June after the Porto Alegre court rejected his request for a Super Court review. As a result, it is likely that former President Lula da Silva will remain in jail through the October election. That said, in early July, an appeals court judge accepted a habeas corpus from former President Lula’s Workers Party and ordered former President Lula to be freed. However, a number of other Brazilian judges subsequently blocked the release order. Meanwhile, Congress approved funds to pay defaulted loans of Venezuela and Mozambique made by the Brazilian Development Bank and Credit Suisse. These loans, guaranteed by previous Brazilian administrations, were originally used to pay Brazilian construction firms that performed work in the two countries. If Brazil had decided not to honor those loans, Moody’s Investors Service noted that they could have negatively affected Brazil’s sovereign risk rating. In late May, truckers across Brazil went on strike to protest rising diesel prices by Petrobrás (Brazil’s state-controlled oil producer), which had been increasing almost on a daily basis since July 2017 as the company started to allow the market to set the price of fuel. The strike made commerce across all industries very challenging. After 10 days, the government capitulated and agreed to subsidize the cost of diesel at the pump by 12% for 60 days, give truckers more government contracts, and allow truckers to pay less in tolls. As a result of the strike, Pedro Parente, the chief executive officer of Petrobras, resigned. In June, Brazil’s central bank began to intervene in the foreign exchange market to support the Brazilian real given increased volatility from the truck strike and lower consumer confidence.

Industrial & Capacity Update

During the quarter, Royal Golden Eagle, a Singaporean based manager of resource-based manufacturing companies with global operations, announced that it entered into an agreement with Lwart Group to acquire 100% of Lwarcel Celulose’s assets in São Paulo including its 250,000 MT/year bleached eucalyptus kraft pulp mill. In June, Brazil’s anti-trust agency CADE approved the acquisition. Meanwhile, the US Federal Trade Commission approved Suzano’s acquisition of Fibria. CADE approval is still pending. In June, Duratex announced a joint venture with Lenzing, a leading global producer of specialty cellulosic fibers, to build a new dissolving wood pulp mill in the state of Minas Gerais, within the Triângulo Mineiro region, close to São Paulo. The annual capacity of the mill is expected to be around 450,000 MT and the initial cost of the mill is estimated at around US\$ 1.0 billion. In addition to cash, Duratex will contribute 43,000 hectares of eucalyptus forests to the joint venture. A final decision on whether the mill will be built will occur in the

second half of 2019 and production is expected in 2022. Meantime, Suzano exercised its option to acquire around 20,000 hectares of timberland in São Paulo from Duratex for R\$ 749.4 million.

Brazilian forest products and timber markets

The price of pine timber in Brazil was generally positive during the quarter. Through the end of April, pulpwood (8-18 cm) in Parana State increased 1.9% quarter-over-quarter, but declined -1.7% year-over-year in local currency terms. Small sawtimber (18-25 cm) increased 1.1% quarter-over-quarter and 1.4% year-over-year while large-diameter sawtimber (25-35 cm) increased 0.3% quarter-over-quarter and 0.8% year-over-year. Veneer logs (+35 cm), used primarily for export-oriented softwood plywood, increased 2.6% quarter-over-quarter and 5.5% year-over-year (Figure 17). The price of larger diameter sawtimber continues to be driven by exports, particularly plywood and lumber.

Wood charcoal, which is used to produce pig iron which in turn is used to make steel, has also started to improve after a number of years of being challenged due to a supply/demand imbalance. In Q2, charcoal prices in Minas Gerais increased 21.2% quarter-over-quarter and 65.7% year-over-year and have continued a strong upward trajectory into early Q3, given lower charcoal supply (e.g., fewer producers as a result of the downturn) and continued improvement in durable goods such as automobiles (Figure 18, left axis). Charcoal pricing is normally reflected in the price of eucalyptus stumpage (Figure 18, right axis). In Q2, Minas Gerais eucalyptus prices increased 4.5% quarter-over-quarter and 0.3% year-over-year.

Figure 17. Pine Sawtimber Stumpage Prices in Paraná State, Brazil. Source: STCP.

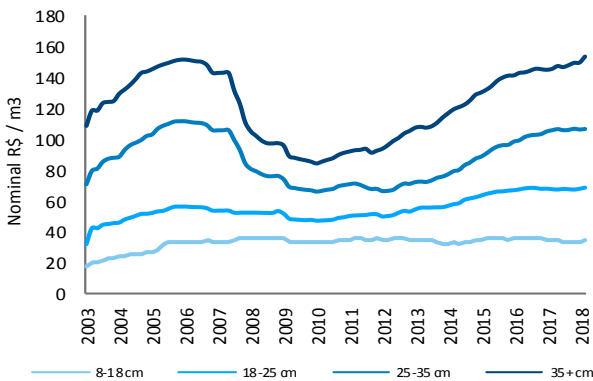
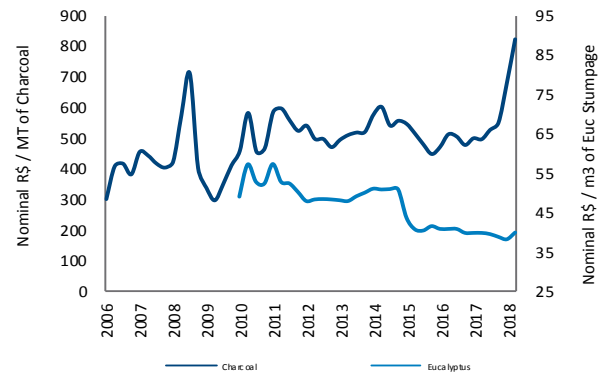


Figure 18. Charcoal and Eucalyptus Stumpage Prices in Minas Gerais, Brazil.

Sources: Associação Mineira de Sicultura; Poyry Silviconsult.



Meantime, eucalyptus pulpwood prices declined -0.4% quarter-over-quarter (ended April) and -0.7% year-over-year on a countrywide basis (Figure 19).

The price of pine resin, a secondary product that can be collected from pine plantations between harvests and is used in the production of synthetic rubber, glues, adhesives, printer inks, and other products, declined during Q2. Mixed tropical pine resin declined -2.0% quarter-over-quarter while slash pine resin declined -0.9% quarter-over-quarter (Figure 20).

Figure 19. Brazil Eucalyptus Pulpwood (8-18 cm) Stumpage Prices. Source: STCP.

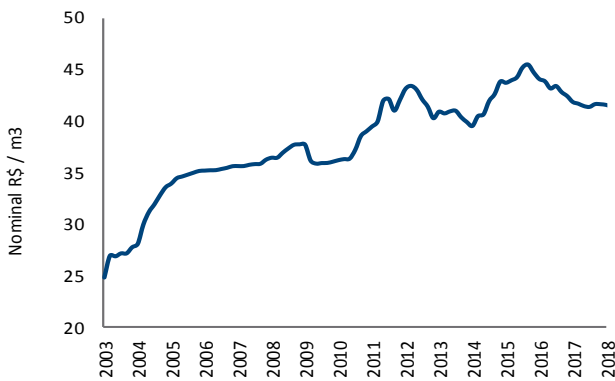
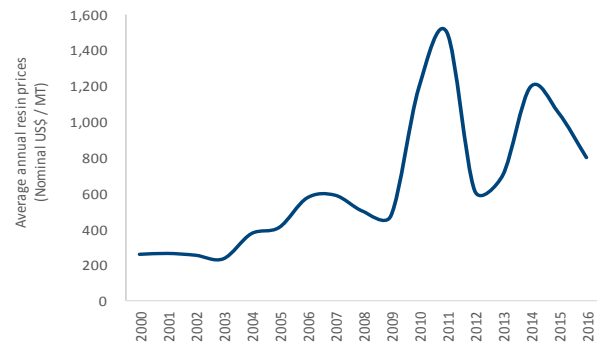


Figure 20. Average Annual Resin Prices in Brazil. Source: Associação dos Resinadores do Brasil



View from the Ground

TIG’s Brazilian regional foresters regularly report on conditions that impact wood pricing in their operating areas. Despite a weak May across all industries given the Brazilian truckers strike, improving Brazilian economic conditions have resulted in better timber conditions in most Brazilian states.

In Minas Gerais, demand for timber continues to increase resulting in higher stumpage prices. Through May, automobile production, a significant driver of pig iron production, has increased 12.1%. Meanwhile, pulp demand remains robust (up 10.3% year-to-date according to Ibá, the Brazilian Tree Industry Association) with mills looking for timber.

In São Paulo (Itapeva region), demand for pulpwood (partially due to an improving packaging market) and sawnwood remain strong. Although shipments of corrugated board, which are used to package a variety of goods, have declined -0.3% year-to-date, this is mostly due to a weak May as shipments declined -19.7% year-over-year due to the truckers’ strike (through April, shipments were up 5.0%). With respect to sawnwood, demand continues to increase, rising 3.9% year-to-date according to Ibá. That said, pulpwood supply still remains elevated as the large area of new plantations established in 2007-2009 have started to reach harvestable age.

Similar to the other regions, Parana is benefiting from improving economic fundamentals and timber demand. In Guarapuava, demand has improved with many companies increasingly looking to purchase wood. That said, the area is faced with a surplus of standing pulpwood similar to the situation in São Paulo.

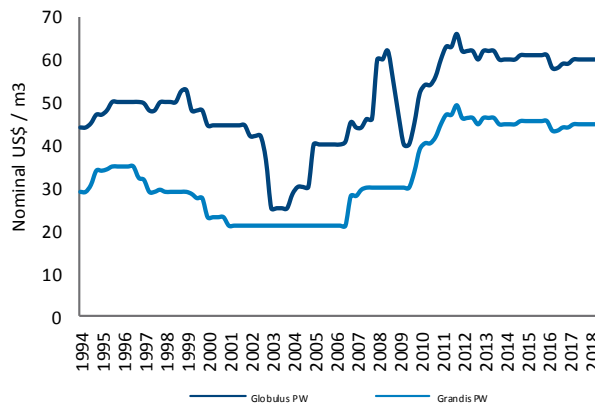
In Santa Catarina, timber demand continues to improve, but timber supply remains elevated as tree plantations established around the same time are beginning to be harvested. Moreover, timber demand is concentrated among a limited number of buyers, which tends to make it difficult for timberland owners to increase prices.

Uruguay

In Q1, Uruguay’s real GDP increased 2.2% year-over-year versus 2.0% year-over-year growth in Q4. Commercial activities increased 4.0% year-over-year while transportation increased 6.7% year-over-year. Gross fixed capital formation declined -2.2% year-over-year in Q1 versus a decline of -6.3% year-over-year in Q4 while household spending increased 2.8% year-over-year versus an increase of 4.6% year-over-year in Q4. Exports increased 4.6% year-over-year versus an increase of 7.0% year-over-year in Q4 while imports increased 3.7% year-over-year versus an increase of 6.0% year-over-year in Q4. During Q1, the Uruguayan peso slightly depreciated around -0.1% year-over-year.

In Uruguay, E. globulus and E. grandis prices were flat quarter-over-quarter and year-over-year in Q2 (Figure 21).

Figure 21. Uruguay E. globulus and E. grandis Pulpwood Prices (Nominal US\$ / m3). Source: Litenco.



During the quarter, the Government of Uruguay received bids from three investors looking to design, build, finance, and maintain a 273-kilometer rail line with annual freight capacity of 4.5 million MT connecting the city of Paso de los Toros and the port of Montevideo. The development of the new rail line is part of the agreement that the government has with UPM, which is currently evaluating a new pulp mill in Paso de los Toros with an annual capacity of about two million MT of eucalyptus market pulp.

View from the Ground

TIG’s local staff regularly report on conditions that impact wood pricing in their operating areas. In Q2, pine sawlog prices were stable given steady export demand, particularly from China. Meanwhile, there is increased competition for eucalyptus pulpwood given the potential for a new UPM pulp mill. A number of companies have been aggressively bidding for properties in order to convert them into eucalyptus pulpwood.

Chile

In Q1, Chile’s real GDP increased 4.2% year-over-year following 3.3% year-over-year growth in Q4. Mining increased 19.3% year-over-year with copper increasing 20.6% year-over-year while retail increased 6.0% year-over-year. That said, agriculture declined -2.3% year-over-year. Meanwhile, gross fixed capital formation increased 3.6% year-over-year,

government spending increased 2.7% year-over-year, and consumer spending increased 3.9% year-over-year. Exports increased 7.2% year-over-year while imports increased 6.1% year-over-year. Exports increased despite a 5.0% sequential appreciation in the Chilean peso versus the US dollar in Q1.

On the industrial front, Arauco intends to proceed with its MAPA project, a new 1.56 million MT/year bleached eucalyptus kraft pulp line (line No. 3) at its Horcones mill in central Chile. The company will shut line No. 1, which produces bleached eucalyptus kraft and was built in the 1970's, and will revamp line No. 2, which produces softwood pulp. The new project is expected to begin production in 2021 and produce around 2.1 million MT/year of bleached eucalyptus kraft pulp. In addition, Arauco is focused on the conversion of its bleached softwood kraft and bleached eucalyptus kraft Valdivia mill into dissolving pulp with production expected to begin in October 2019.

Argentina

In Q1, Argentina's economy improved with real GDP increasing 1.1% quarter-over-quarter versus 1.0% growth quarter-over-quarter in Q4. On a year-over-year basis, real GDP increased 3.6% versus 3.9% growth year-over-year in Q4. Argentina's year-over-year improvement is the result of a 4.1% year-over-year increase in private consumption and 18.3% year-over-year increase in investments, largely driven by notably stronger machinery and equipment (27.6% year-over-year) and construction (11.9% year-over-year). During Q1, exports increased 6.4% year-over-year, partially as the Argentinian peso depreciated -25.5% year-over-year (-12.1% sequentially) against the US dollar.

On the economic front, extreme drought conditions have negatively impacted growth by destroying around 30% of the country's estimated soybean and corn crops. Due to the drought, President Mauricio Macri expects a 1% reduction in economic growth in 2018 with GDP slightly exceeding 3%. Beginning late April, the Argentinian peso experienced sharp declines. To stem the declines, Argentina's central bank, Banco Central de la Republica Argentina, used reserves to support the peso and significantly increased interest rates. The International Monetary Fund ("IMF") also agreed to a US\$ 50 billion stand-by package with Argentina, which included conditions that the central bank would allow the level of the peso to be determined by market forces. That said, the central bank continued to periodically sell reserves to support the peso, which ultimately resulted in the resignation of Federico Sturzenegger, President of the central bank. In late June, Argentina used US\$ 7.5 billion of the US\$ 50 billion in IMF funds to finance its budget. Meanwhile, in late June, Argentina experienced a nationwide strike organized by the country's main unions calling for wage discussions after inflation increased more than expected at the time that the labor agreements were originally signed. This follows another strike earlier in June in which trucker drivers blocked streets in Buenos Aires.

On the industrial front, CMPC announced that it intends to install a new 54,000 MT/year tissue machine at its Zárate mill, in Buenos Aires. The new machine is expected to cost around US\$ 130 million and startup is expected at the end of 2019.

Guatemala

In Q1, Guatemala's real GDP increased 2.0% year-over-year versus 2.9% year-over-year growth in Q4. All industries generally improved versus the prior year except mining & quarrying which declined -54.8% year-over-year. Exports declined -2.6% year-over-year in Q1 versus an increase of 0.4% year-over-year in Q4 while imports declined -2.4% year-over-year in Q1 versus an increase of 1.6% year-over-year in Q4. During Q1, the Guatemalan quetzal appreciated around 0.9% year-over-year.

Europe

In the euro zone, Q1 real GDP increased 0.4% quarter-over-quarter as compared to 0.7% quarter-over-quarter growth in Q4. Year-over-year, real GDP increased 2.5%. On an individual country basis, real GDP growth was flat in Spain quarter-over-quarter, but declined in France, Germany, and Italy. Gross fixed capital formation grew 0.5% quarter-over-quarter in Q1 versus growth of 1.3% quarter-over-quarter in Q4. Personal consumption increased 0.5% quarter-over-quarter, better than the prior quarter, while government spending was flat, worse than the prior quarter. Unemployment remained flat at 8.4% in May versus April.

Meantime, European net exports (exports less imports) declined year-over-year. In May (latest month reported), exports declined -0.8% year-over-year while imports increased 0.7% year-over-year, resulting in a euro zone trade surplus of €16.5 billion versus a surplus of €19.3 billion in May 2017.

Estonian forest products and timber markets

Sawlog prices in Estonia generally improved over the last few months. Pine sawlog prices (latest data available May 2018) declined -1.5% from three months earlier, but increased 19.9% year-over-year. Birch sawlog prices increased 9.2% from three months earlier and 18.9% year-over-year (Figure 22).

Estonian pulpwood prices also increased. Pine pulpwood prices (latest data available May 2018) increased 45.3% from three months earlier and 82.0% year-over-year while birch pulpwood prices increased 41.1% from three months earlier and 90.6% year-over-year (Figure 23). Prices jumped given strong demand and lean log decks, partially given less wood flow from Sweden due to challenging weather conditions earlier in the year.

Figure 22. Estonia Sawlog Prices (Nominal € / m3).

Source: RMK (Estonia State Forest Agency).

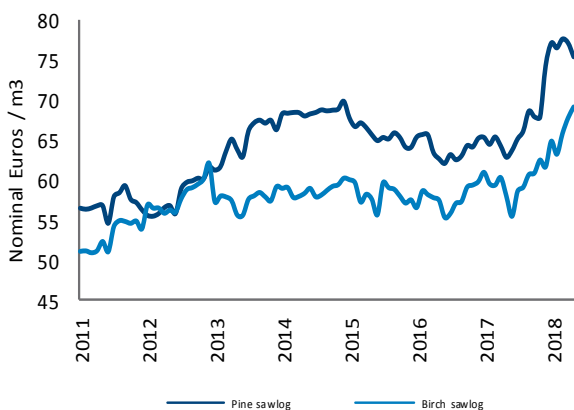
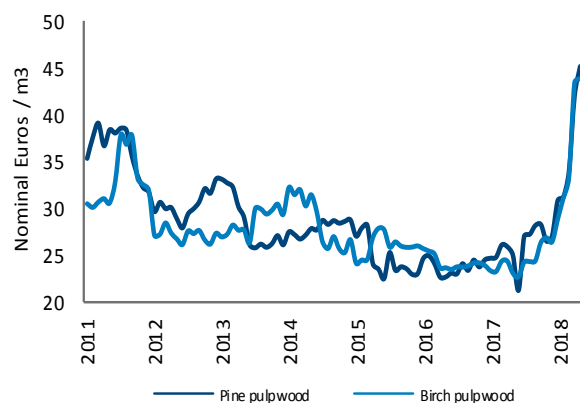


Figure 23. Estonia Pulpwood Prices (Nominal € / m3). Source: RMK (Estonia State Forest Agency).



South Africa

In Q1, South Africa's real GDP declined -2.2% quarter-over-quarter following an increase of 3.1% quarter-over-quarter in Q4, the worst decline in nine years. Agriculture, forestry, and fishing declined -24.2% quarter-over-quarter (partially due to less rainfall), mining declined -9.9% quarter-over-quarter, and manufacturing declined -6.4% quarter-over-quarter.

In May, a South Africa judicial commission began investigating allegations that members of the Gupta family worked with President Jacob Zuma and his son to steal billions of rand from state coffers. Separately, a fraud, racketeering, and money laundering case against former President Zuma has been adjourned until late July. Meanwhile, the ruling African National Congress ("ANC") party is exploring whether land expropriation without compensation is permissible under the current constitution. If not, the ANC is recommending to amend the constitution to allow for the expropriation of white-owned land. Given attacks and discrimination stemming from land expropriation, more than 200 white farmers have applied for humanitarian visas in Australia.

On the industrial front, Mondi acquired the Draycott and Greytown Timber Plantations in KwaZulu-Natal province.

South African forest products and timber markets

In May, lumber prices increased 0.7% versus the prior three months and 1.0% from May 2017, as measured by the South African Lumber Index, a composite price series (Figure 24).

Softwood log prices were positive (Figure 25). Sawlogs in South Africa are categorized into A, B, C or D grades, with A grade logs being the smallest and D grade logs being the largest. In nominal terms in Q1 (latest data available): A grade logs increased 4.7% for the quarter and 10.5% year-over-year, B grade logs increased 1.7% for the quarter and 7.0% year-over-year, C grade logs rose 2.0% for the quarter and 7.1% year-over-year, and D grade logs declined -1.0% for the quarter, but increased 3.5% year-over-year.

Despite the aforementioned price gains, it is worth noting that annual inflation in South Africa is 4.4%, so in real terms most of the gains are less notable and in some cases even negative (i.e., A grade logs: 5.8% real year-over-year, B grade logs: 2.5% real year-over-year; C grade logs: 2.6% real year-over-year, and D grade logs: -0.9% real year-over-year). Meanwhile, in Q2, the rand depreciated -5.5% sequentially against the US dollar (Figure 26) and -2.6% sequentially against the Euro (Figure 27).

Figure 24. South Africa Lumber Index.

Source: Crickmay and Associates.

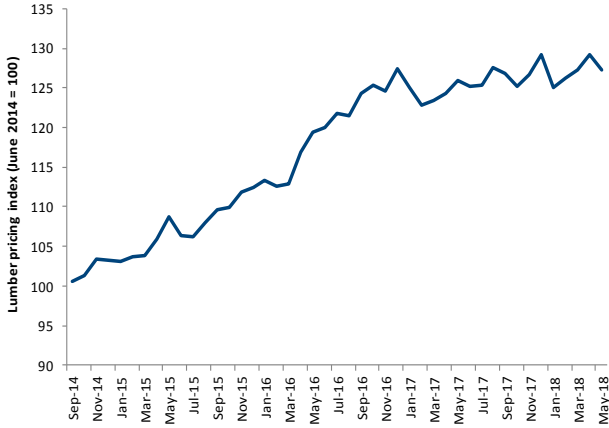


Figure 25. South Africa Pine Sawlog Prices.

Source: Crickmay and Associates.

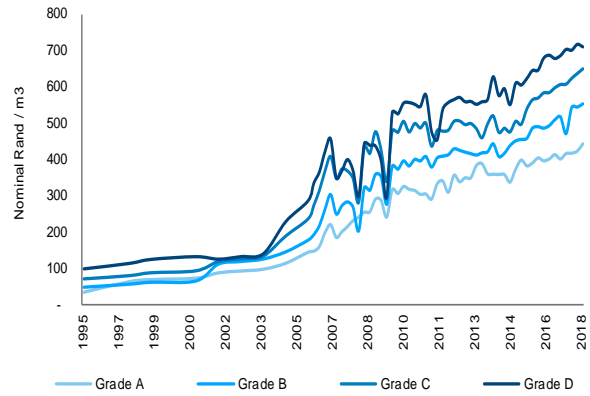


Figure 26. South Africa Rand to US\$ Exchange Rate.

Source: Federal Reserve Bank of St. Louis.



Figure 27. South Africa Rand to Euro Exchange Rate.

Source: Bloomberg.



New Zealand

In Q1, New Zealand’s real GDP increased 0.5% quarter-over-quarter versus 0.6% quarter-over-quarter growth in Q4. Exports slightly declined -0.1% quarter-over-quarter on weakness in both meat (-8.9% quarter-over-quarter) and chemicals (-6.7% quarter-over-quarter) while imports increased 1.2% quarter-over-quarter due to capital goods. In Q1, the New Zealand dollar appreciated 4.3% quarter-over-quarter against the US dollar (Figure 28).

New Zealand timber markets

New Zealand A-grade export logs increased 3.0% quarter-over-quarter in March to NZ\$ 165/m³ from NZ\$ 160/m³ (Figure 29) given declining port inventories and steady demand in China, New Zealand’s largest export market, as well as good demand from India. Domestic structural logs used for construction (S1 and S3) were positive given steady demand for domestic lumber (Figure 30) and limited supplies in certain regions.

Figure 28. NZ Dollar / US\$ Exchange Rate. Source: Federal Reserve Bank of St. Louis.



Figure 29. NZ Export Log Prices. Source: New Zealand Ministry for Primary Industries.

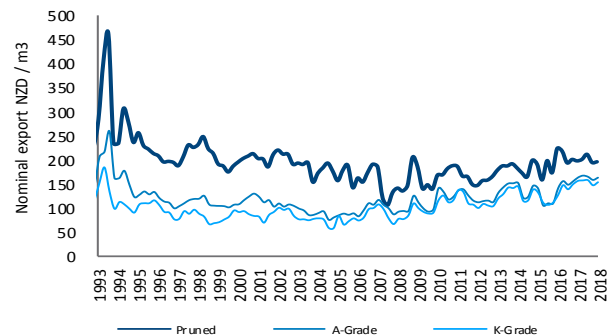
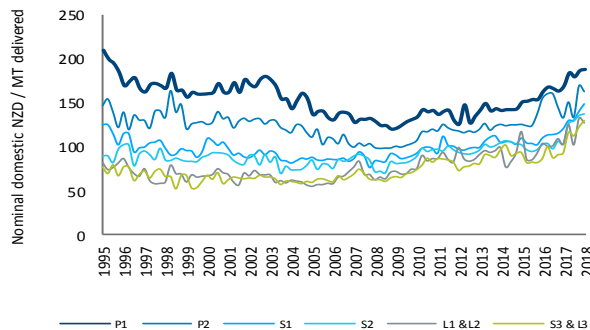


Figure 30. New Zealand Domestic Log Prices.

Source New Zealand Ministry for Primary Industries.



Australia

In Q1, Australia’s real GDP increased 1.0% quarter-over-quarter versus growth of 0.5% quarter-over-quarter in Q4. Mining increased 2.9% quarter-over-quarter due to oil & gas, coal, and iron ore while manufacturing increased 2.4% quarter-over-quarter due to increased demand for meat products. Agriculture, forestry and fishing declined -1.7% driven by weakness in grains. Meantime, exports increased 2.4% quarter-over-quarter while imports increased 0.5% quarter-over-quarter. In Q1, the Australian dollar appreciated around 2.2% quarter-over-quarter (Figure 31).

Australian timber markets

Softwood roundwood prices increased 6.2% quarter-over-quarter to US\$ 86/odmt (“oven dry metric ton”) from US\$ 81/odmt in Q4 (Figure 32) partly due to steady export demand from China. Hardwood roundwood prices increased 3.0% quarter-over-quarter to US\$ 102/odmt from US\$ 99/odmt in Q4 (Figure 33). Both softwood and hardwood chips moved higher in Q1, increasing 11.1% and 8.5%, respectively. Australia is the second largest exporter of chips to China following Vietnam.

Figure 31. Australia Dollar to US\$ Exchange Rate.

Source: Federal Reserve Bank of St. Louis.



Figure 32. Australian Softwood Pulpwood Prices.

Source: Wood Resource Quarterly.

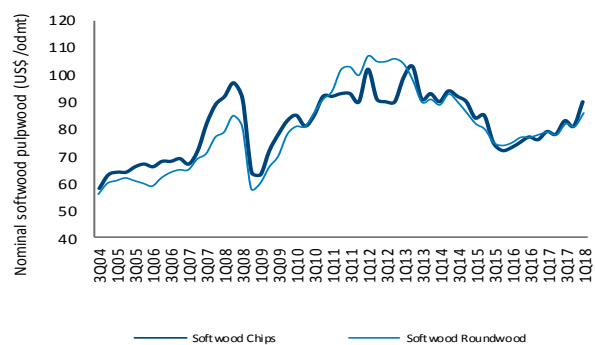
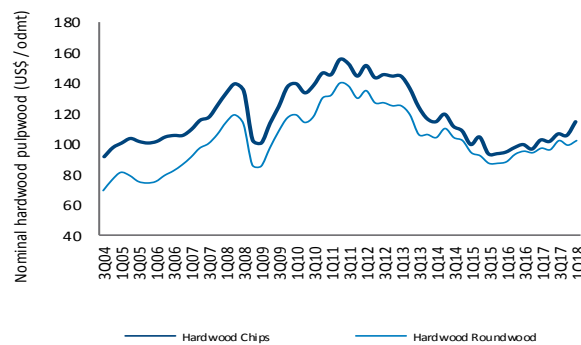


Figure 33. Australian Hardwood Pulpwood Prices.

Source: Wood Resource Quarterly.



Global Pulp and Paper Markets

During Q2, Bleached Hardwood Kraft Pulp (“BHK”) prices in Europe, a key benchmark, increased 3.5% quarter-over-quarter and 33.4% year-over-year, averaging around US\$ 1044/MT (Figures 34 & 35). Prices improved largely due to unexpected mill downtime and steady demand.

Specifically, the Brazilian truckers’ strike, which began on May 2 and lasted for 11 days, depleted pulp inventories and forced many pulp and paper operations to cease production. The total production loss is estimated to be between 200,000-400,000 MT. Meanwhile, Chinese mills are increasing their inventories of hardwood pulp due to restrictions on imports of recovered paper and soon-to-be-implemented new rules that require that the China Certification and Inspection Group perform 100% on-site live inspections of recovered paper before it is shipped to China. After the summer, hardwood pulp demand has the potential to further increase as Chinese paper production accelerates.

The price of BSK in Europe, a bellwether of the pulp and paper sector, averaged around US\$ 1159/MT, up 9.8% versus the prior quarter and 34.7% year-over-year (Figures 34 & 35).

During the quarter, softwood pulp pricing increased given steady demand, maintenance downtime in North America which reduced supply, and as softwood producers looked to maintain a positive price spread with hardwood pulp. The improvement in demand is partially due to restrictions on imports of recovered paper (the Chinese government set a strict 0.5% contaminant rule on imports of old corrugated containers). On the supply front, North American pulp producers took around 160,000 MT of maintenance downtime during the quarter. Going forward, softwood supply could increase as SCA began production at its expanded Östrand pulp mill. The company increased the mill’s production to 900,000 MT of BSK from 430,000 MT with full production targeted to occur in 2020.

Figure 34. Global BSK and BHK Pulp Prices over Time.

Source: FOEX.

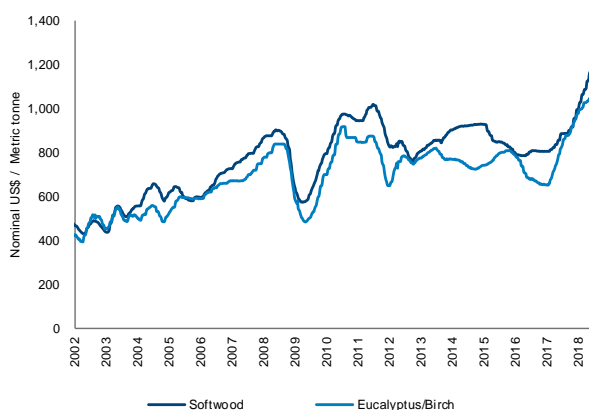


Figure 35. Global BSK and BHK Pulp Prices Recent Performance. Source: FOEX.



Baltic Dry Index

In Q2, the Baltic Dry Index, which provides a benchmark for the price of transporting major raw materials including grains, coal, and iron ore by sea, increased 31.3% during the quarter (Figures 36 & 37). At a value of 1385 on June 29, 2018, the index remains well below its peak of 11,793 reached in May 2008.

Figure 36. Baltic Dry Index Performance over Time.

Source: Bloomberg.

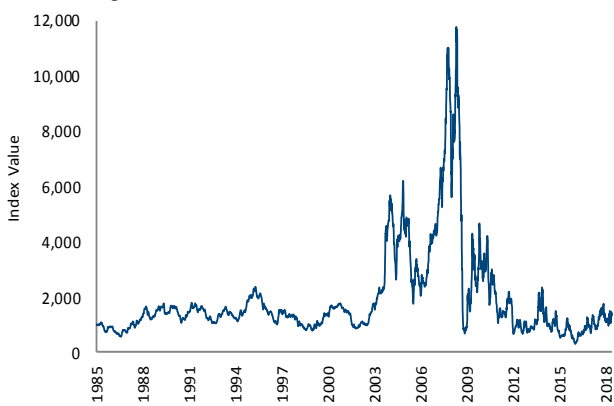
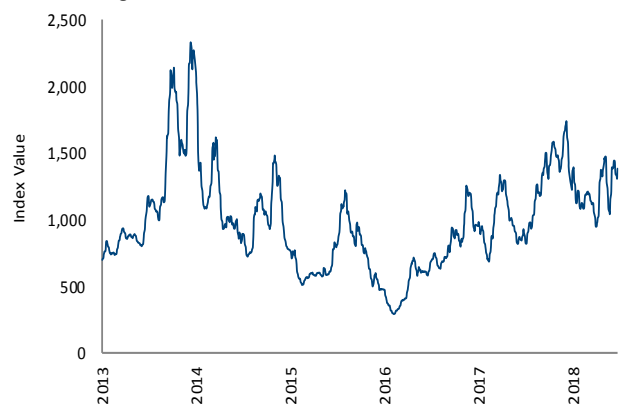


Figure 37. Baltic Dry Index Recent Performance.

Source: Bloomberg.



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