

The Phaunos Timber Fund plc (ticker code: PTF-L)

The 'Regular Investor', which actions key recommendations on investRcentre.com website, is buying the *Phaunos Timber Fund (PTF-L)* as of Friday's closing price (22nd Jan 2010). It is listed and traded on the London Stock Exchange and is quoted in dollars. The price has crept up recently from \$0.67 a share when we first covered it to \$0.73 a share now. Nonetheless, at \$0.73, the attractions of this fund remain considerable;

- The fund is at a 26% discount to the underlying net asset value.
- Lumber (timber) prices are recovering with the global economy
- Timber is an alternative and environmental-friendly asset class
- The fund has no debt and
- The fund has good geographical exposure including to emerging markets

Phaunos Timber Fund plc is a quoted investment company. This means that it is in effect a fund but it is structured as a company. Hence, to gain exposure to the company you must buy shares off another investor in the market place like you would any other company and via your stockbroker. Although the shares are quoted in dollars, as an investor, you have minimum dollar exposure as the fund has only 7% of its assets in US forestry.

The company specialises in investing in timber globally mainly directly in forest acreage but also (more modestly) through investments in other companies operating in the sector. Timber, as an asset class, has done as well as, if not better than, equities and property over the long term. According to the stockbroker Collins Stewart, the NCREIF Timberland Index (National Council of Real Estate Investment Fiduciaries) averaged returns of 15% annually since 1987 compared to 9% for the S&P 500 Equity Index. You can google NCREIF timberland index and there is plenty to read up on timber investing on the internet. In addition, timber returns have a low correlation with other asset classes which gives any portfolio added balance.

A More Solid 'Environmental' Theme

Timber as an investment also ticks the 'environmentally-friendly' box. If I am going to buy into the carbon emissions, new energy and climate change themes, I would rather do it through an asset class that has proven over many years to produce good returns. I have little faith in many of the funds (ETFs or otherwise) that chase new technologies in these themes and which are being promoted to investors as the next best thing. Quite simply, most of them are venture capital-type vehicles, investing in unproven companies in unproven niche sectors.

Phaunos Timber was listed on the London market in December 2006 raising \$115 million at a dollar a share from investors at that time. It raised a further \$370 million in July 2008 at \$1.04 a share. The managers of the fund, Four Winds Capital Management, charge a hefty 1.5% annual management fee and can benefit from a 20% slice of any annual returns over 8%, which is overly generous in my view but the exposure to timber and the discount on offer is incentive enough for me.

Decent Emerging Market Bias

There is no debt in the company, so no financial risk for investors to worry about. The geographic spread of the company's assets (owned or committed to buying) is US 7%, Europe 23%, Latin Americas 36%, China 29% and other emerging markets 6%. So the fund offers good exposure to the faster developing regions of the globe. The managers appear to have taken a cautious approach to investing the cash as it is still being invested and most likely at decent prices given the global economic downturn.

The company posted an end of year activity update in January announcing a number of significant investments in 'standing timber' assets in Brazil and New Zealand in December.

Big Discount a Key Reason to Buy

Aside from the attractions of timber as an asset class, the other significant attraction is the value on offer at present. The shares are currently trading at a price of \$0.72-\$0.73 a share against a net asset value of \$0.99 a share, representing a 26% discount. If the company's forestry assets can deliver annual returns of even 8% from here then on a 5-year view the net asset value would grow to \$1.50 a share. The share price would likely follow and could potentially at least double in value over this timeline. More information can be found on the company's website www.phaunostimber.com.

Recovery in Lumber Prices a Provides a Good Tailwind

Lumber (timber) prices are an important piece of the jigsaw. Weak prices make it difficult to harvest timber from any forestry land the company owns. Lumber prices have been very weak this past few years no doubt reflecting in particular the huge housing and general construction downturn.

Thanks to the excellent fullermoney.com website, I have now sourced a medium term lumber price chart. Clearly, weakness in lumber prices will hold back the value of forestry assets and the severe weakness in lumber prices has no doubt contributed significantly to the weak performance of the Phaunos Timber plc share price. While I have no idea where lumber prices are going from here, it is nonetheless encouraging that lumber prices are recovering, and appear to be poised for fresh upward moves. If so, they should provide a tailwind for related assets dependent on strong lumber prices in the future. Apologies for the poor quality of the chart but it's the best I can do without access to the original.

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