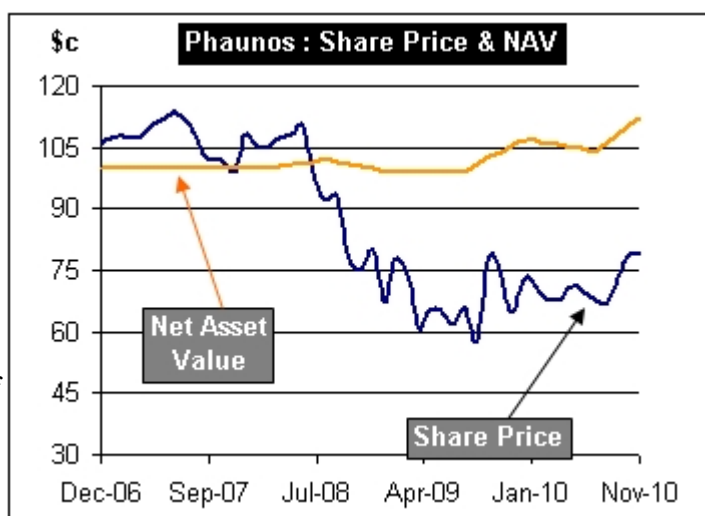


## Update on the Phaunos Timber Fund plc - Dividend Policy a Likely Trigger

30<sup>th</sup> Oct 2010

Phaunos Timber Fund plc (PTF-L) provided an update to the market yesterday so I thought it would be timely to revisit the investment case. As a reminder, timber represents an entirely separate asset class and one that is generally uncorrelated to equities or property. Timber gains value not because the economy is doing well but because it grows, and the more it grows the more value it attains. And over the long term, timber has delivered returns equal to if not slightly better than equities. The eventual sale price is important but it is also local so that a weak timber price in the US does not automatically mean a weak timber price in Brazil. Geographic balance in a timber fund has, therefore, added attractions and the Phaunos Timber Fund plc scores well in that regard.



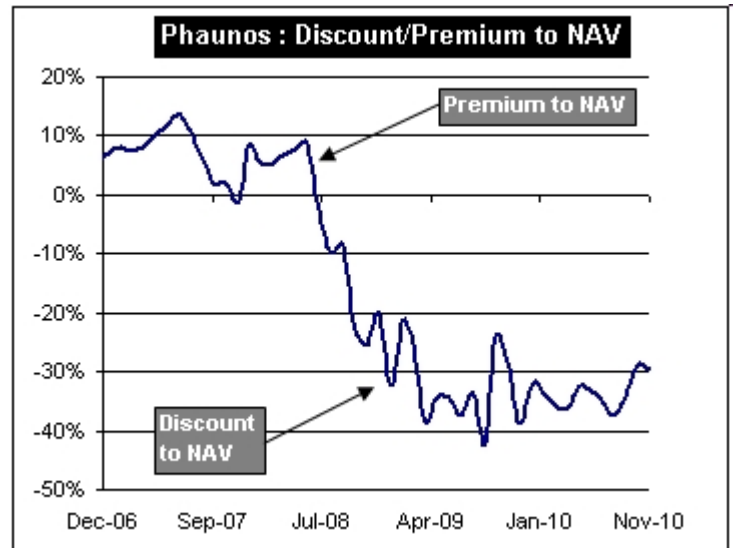
Phaunos Timber was launched in late 2006 and has raised a total of \$490 million. In the early years, as the chart shows, the net asset value barely moved reflecting the fact that the monies were invested at a slow rate. The monies are now nearly fully invested with the result that the net asset value (NAV) should start growing. In addition, the management statement makes it clear that some harvesting has already begun which will provide cash flows to fund a dividend. Management is to define the dividend policy at the full year results (likely around March

Project	Region	Stake	Proportion of NAV
Matariki Forestry	New Zealand	Minority	22%
Mata Mineira	Brazil	100%	15%
Eucateca SA	Brazil	100%	13%
Green Resources	East Africa	Minority	13%
Aurora Forestal	Uruguay	Minority	5%
Greenwood Tree Farm	USA	Minority	5%
Pradera Rofa	Uruguay	100%	5%
Green China Forestry	China	100%	5%
National Timber Partners Fund	USA	100%	2%
Forest Enterprise	Russia	100%	2%
Caldrey SA	Uruguay	100%	1%
Cash Resources			12%
<b>Total Portfolio</b>			<b>100%</b>

2011). Phaunos provides an updated NAV every six months (with the Interim & Annual Reports). The current official NAV is \$1.04 as of end June last. But I have subjectively pencilled in \$1.12 for end October on the basis that the dollar has weakened and growth in its timber assets. Phaunos' timber portfolio is global and as the dollar weakens the value of the portfolio would rise in dollar terms.

The Phaunos Timber investment case has several attractive attributes;

- Timber provides the prospects of decent long term returns well above inflation (similar to equities)
- As an alternative asset, it provides balance to a risk-asset portfolio i.e. over time returns should be positive but uncorrelated to equities or property helping to smooth out returns from year to year
- Phaunos' geographic spread of timber assets is attractive with good exposure to New Zealand, Brazil, Uruguay and East Africa i.e. only minor dependence on developed economies.
- In addition, the timber assets are at varying degrees of maturity facilitating a steady build up in cashflows from here.
- With the fund's monies only now fully invested, growth in the NAV should be steady from here.
- As the assets have been bought through out the downturn the fund could benefit from rising land prices in addition to the growth in timber values.
- The company has no debt
- The shares, at \$0.79, remain at a substantial discount to the NAV, still some 30% by my estimates. That should surely change when the dividend becomes more meaningful or when the NAV growth becomes more consistent. Management comments yesterday that a dividend policy will be set at the publication of the full year results to Dec 2010 is significant in that regard.



All in all, the case for buying a holding in Phaunos Timber Fund plc remains intact.