Phaunos Timber Fund Limited - PTF Forthcoming Continuation Vote Update
Released 08:47 08-Jun-2017

RNS Number : 5261H
Phaunos Timber Fund Limited
08 June 2017

Phaunos Timber Fund Limited

("**Phaunos**" or the "**Company**")

8 June 2017

Forthcoming Continuation Vote Update

At the Annual General Meeting of Phaunos Timber Fund Limited ("Phaunos" or "the Company" or "the Fund") to be held on 19 June 2017, an ordinary resolution will be proposed to shareholders with the objective of a five-year continuation of the Company.

In 2014 the Board took a decisive step in replacing the Investment Manager with Stafford Capital Partners Limited ("Stafford") to resolve the problems of the initial years of the Fund. Stafford's remit was to improve the quality and balance of the Phaunos portfolio. It is the Board's view that Stafford has acted capably in restructuring the portfolio, and three years later this task has been substantially completed. Phaunos is now cash flow positive, has produced positive NAV returns over the last year and is able to pay sustainable dividends. The targeted real return of the Fund, over the medium term is a yield of between 3% and 5% alongside NAV growth of 3% to 5%.

In discussions with shareholders a number of questions have been asked and the Board believes it should respond publicly for the benefit of all shareholders.

1. What is the Company's intention in relation to its current cash balance?

Phaunos' cash position as at 31 December 2016 was $45.6m, or 15% of the overall NAV.

a) Of this amount, should the Company's continuation be approved, approximately $19.4m will be allocated to dividend payments ($8.9m as the final dividend for 2016 and a targeted total dividend of $10.5m for 2017).
b) Operating costs for 2017 are expected to be in the order of $7.5m. The Company maintains two year's worth of operating costs as a reserve working capital buffer. This amounts to $15m.
c) The Company has declared its intention to continue "to buy back shares on an opportunistic basis". So far, this year, share buybacks have been limited due to existing investors increasing their shareholding and also due to the closed period

up until the release of Phaunos' annual accounts. Should a similar level of buybacks to 2016 be maintained, the remaining available cash may be applied to further share buy backs.

These allocations absorb significantly all of the cash held by Phaunos. The Company anticipates that it will be cash generative during 2017; however, this is likely to be insufficient on its own for any meaningful investment into new assets.

2. Is the portfolio adequately diversified?

Currently 46% of the Fund is invested in Matariki Forests in New Zealand. Whilst this may initially seem overweight within Phaunos' portfolio, the asset benefits from an active domestic market for both sawlogs and pulpwood with numerous participants, as well as excellent export markets across South East Asia. Both domestic and export markets are currently very buoyant, with demand and pricing expected to remain firm in the medium term. This is driving the performance of Matariki, which also benefits from operating in a politically stable country.

It is rare to find forestry assets of this quality, geographically diversified within New Zealand with forestry spread across both islands and with access to a diverse range of markets both in terms of product and geography; internally within New Zealand and across a range of other countries.

Matariki contrasts with Phaunos' remaining assets in that, whilst they offer geographic diversification, they typically service a narrower and more local range of markets. The Company's two Brazilian investments, which comprise 21% of NAV, serve as examples of assets which have experienced tough market conditions during the past few years, and which have had more limited flexibility in finding alternative outlets for their wood supply. Phaunos remains open to potential selling opportunities for these properties, but will not make a hasty exit in a down cycle. Stafford have instead focused their efforts on securing sales contracts for wood volumes available from these assets. For Mata Miniera harvested volume in 2017 is expected to more than double from 2016, and there has been encouraging progress towards securing wood sales contracts on Eucateca.

The Company's two Uruguayan assets make up 18% of NAV, and comprise Aurora Forestal, which is a mature pine asset providing steady yields back to the Company, together with Pradera Roja, an immature eucalyptus asset with a low cost base.

The restructuring process undertaken by Stafford has seen the higher risk assets reduced from 36% of the portfolio in June 2014 to 13% at the end of 2016. The opportunity to increase diversification, lower risk and increase yield will remain on the agenda and a focus of the Managers and the Board. While there are likely to be opportunities to rebalance the portfolio further, the existing assets do provide an appropriate level of exposure across different geographies and markets and, perhaps most importantly, the ability to generate revenues capable of supporting Phaunos' targeted yield.

3. Is the Board concerned about the share price discount to NAV and is the current level of discount sustainable?

The Board has always shared shareholders' concerns about the level of discount at which the Company's shares trade. Central to the response, in reducing the discount, the Board has focussed on improving the performance of the Company, which has now resulted in providing regular dividends. The Board believes this is one of the reasons for the narrowing share price discount. A thriving company with solid NAV growth combined with regular dividends provide the best basis to ensure a low level of discount.

It is impossible to predict with any certainty Phaunos' share price immediately following a successful continuation vote. The discount at which the Company's shares trade has improved consistently over the past three years. Since December 2016 the discount has closed from 25% to a current level of just 9%, admittedly on the back of relatively small traded volumes. However, we recognise that a major shareholder making public its desire to exit its investment could, in itself, be a drag on the share price until resolved. Nonetheless, with the uncertainty associated with the continuation vote removed, combined with the strong prospects of the Company's future financial performance, we believe that the Company will be in a better position to market itself to new investors. This should create renewed demand for Phaunos' shares from existing and potential new shareholders.

The Board recognises the need to continue to focus on the share price. Share buybacks will continue on an opportunistic basis and the payment of a dividend will be helpful. In addition Stafford have taken steps to improve shareholder communications and marketing. A successful continuation vote will allow them to redouble these efforts to build greater awareness of the opportunities Phaunos offers, which have been hard to articulate until this moment. Now that Stafford has produced an attractive timberland investment proposition, we believe that Phaunos' share price rating should better reflect the income yield and growth which we are anticipating.

4. Has the Board considered making a tender offer?

The Board has considered whether it would be practical to make a tender offer for shares. However, the Company has insufficient cash reserves to support a meaningful offer. In the absence of adequate cash such an offer would require the sale of assets. This holds several challenges, including:

- It can take many months, as a minimum, to conclude the marketing and sale of a timberland asset;
- There are contractual aspects governing the sale of Phaunos' minority holdings. These dictate the scale and process of any sale, and limits the ability of realising this capital within a short time frame;
- Depending on which assets are sold, the portfolio's ability to generate sufficient income to support the targeted dividend yield may be negatively impacted; and
- The size of the Fund would be eroded, reducing the capacity for diversification and potentially making it sub-scale for certain investors.

The Board therefore believes that a tender offer funded by the sale of assets would be value destructive and not in the best interests of all shareholders.

5. Has the Board considered the consequences of winding up the Fund at this point?

In considering whether or not to recommend continuation, the Board discussed the consequences of a wind up. It is not possible to state with any certainty the level of discount that would be suffered on the sale of the Company's assets, or the time scale to sell all of the underlying investments. A similar timber fund has taken several years to complete their realisation process and incurred a significant loss in value.

Given that the fund is now in a position to provide sustainable growth, the Board believes that there is a considerable opportunity in the future of the Fund. Stafford has more than $2 billion of timberland assets under management for institutional clients who have experienced good returns and Phaunos provides a mechanism to access this expertise through a quoted vehicle.

The Board was, and remains, firmly of the view that shareholders' interests are best served by recommending the continuation of the Company rather than its winding up.

In conclusion, the Board has made great efforts to understand the views of all shareholders and recognises that the return expectations and time horizons of shareholders will vary. Our role is to act in the best interests of the Company and its shareholders as a whole. Phaunos' turnaround is now largely complete, the Company is cash flow positive, has produced positive NAV returns over the last year, and is in a position to start paying sustainable dividends. Against this background a five-year continuation is likely to open the door for new investors, and to give all investors the opportunity to benefit from the continued improvements in the Fund's performance that Stafford has delivered.

The Board's recommendation is thus to support a continuation of the Company and all members of the Board who own shares in Phaunos will be voting in favour of this proposal.

We continue to welcome the views of shareholders and to be open to discussions with any shareholder.

Sir Henry Studholme Bt

Chairman

Enquiries:

Stafford Capital Partners Limited (Manager)
Michael Goodfellow, +44 (0)20 7535 4915

Media Enquiries:
Phoenix Financial PR
Gordon Puckey: +44 (0) 7799 767468

Winterflood Investment Trusts (Corporate Broker)
Joe Winkley, +44 (0)20 3100 0301

Phaunos Timber Fund Limited (Chairman)
Sir Henry Studholme

info@phaunostimber.com

Notes to Editors

1. About Phaunos Timber Fund Limited

Established in 2006, Phaunos Timber Fund Limited ("PTF" or "the Company") invests in a concentrated, but diversified portfolio of timberland and timber-related investments. The Company seeks to provide Shareholders with attractive investment returns over the longer term, largely in the form of capital appreciation, but with some income.

PTF is a Guernsey-domiciled authorised closed-ended investment scheme, authorised by the Guernsey Financial Services Commission under section 8 of The Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended) and the Authorised Closed-ended Investment Schemes Rules 2008 made thereunder. The Company's ordinary shares are traded on the Main Market of the London Stock Exchange. www.phaunostimber.com

2. About Stafford Capital Partners Limited

Established in 2000, Stafford Capital Partners ("Stafford") is a leading private markets investment group. It has specialist investment teams working across Real Assets, Private Equity and Credit, and with offices in Austin, Boston, Hanover, London, Sydney and Zurich, has a truly global presence. As at 31 March 2017, Stafford has more than US$4.8 billion under management and advice, with US$2.3 billion in timberland investments. Stafford was appointed as the Manager of Phaunos on 1 July 2014. (www.staffordcp.com)

Stafford's timberland business provides fund management and advisory services to institutions seeking global timberland exposure; this is achieved through pooled investment vehicles and co-investment opportunities in transactions (which are sometimes larger than the capacity of the primary fund). Stafford's pooled funds offer globally diversified portfolios of timberland assets, and are actively managed to take advantage of developing market trends. Stafford presently manages timber investments in Australia, Brazil, Canada, Central America, Chile, New Zealand, the US and Uruguay.
Stafford Capital Partners is a member of the 'Principles for Responsible Investment' (PRI); these Principles are an internationally agreed upon framework, designed to help institutional investors to incorporate Environmental, Social and Governance (ESG) considerations into their investment decision-making and ownership practices. The PRI has acknowledged Stafford as having incorporated a solid framework for ESG considerations into its investment decision process.

The Company's ticker is PTF. www.phaunostimber.com

END

MSCGRGDLUSGBGRI