

CORTON GLOBAL TIMBER FUND

SPECIAL REPORT – September 20, 2021

Forest Companies Trading at Very Low Valuations

Event: Despite reporting record earnings in the last four quarters and building very strong balance sheets with large cash reserves, **most of the companies held in the Corton Global Timber Fund are trading at ridiculously low multiples.** In addition, the Canadian companies in the Fund are trading at multiples that are approximately 50% lower than the U.S. forest companies.

Back to Basics – Over the past several years, most forest product analysts have relied solely on Enterprise Value-to-EBITDa (EV/EBITDa) multiples to determine “target prices”. However, with the strong balance sheets (i.e. no or little debt and lots of cash), EV/EBITDa multiples have become less relevant. **We believe investors should be more focused on traditional valuation metrics, including; price-to-earnings, and price-to-bookvalue as well as historic multiples of EBITDa.** Table 1, shows the P/E, P/BV, and EV/EBITDa multiples for the top 10 holdings in the Corton Global Timber Fund.

Table 1 – Forest Company Valuations

Company	Price 09-17-21	2021e *				Multiple		
		EPS	EBITDa (mils)	BVPS	EV (mils)	P/E	Price/ BVPS	EV/ EBITDa
Canfor	26.25	13.46	2,737	34.38	1,759	2.0X	0.8X	0.6X
Canfor Pulp	6.48	1.74	235	9.92	329	3.7X	0.7X	1.4X
Interfor	28.37	15.91	1,405	29.97	1,324	1.8X	0.9X	0.9X
Stella-Jones	43.60	3.94	447	23.89	3,202	11.1X	1.8X	7.2X
West Fraser (\$US)	78.01	28.28	4,767	79.06	6,217	2.8X	1.0X	1.3X
AVERAGE						4.3X	1.0X	2.3X
Boise Cascade (\$US)	54.15	18.92	1,094	38.33	1,589	2.9X	1.4X	1.5X
Louisiana-Pacific (\$US)	60.01	12.75	1,841	24.86	5,156	4.7X	2.4X	2.8X
PotlatchDeltic (\$US)	53.02	8.45	844	21.8	3,894	6.3X	2.4X	4.6X
Rayonier (\$US)	37.33	0.66	320	14.18	5,717	56.6X	2.6X	17.9X
Weyerhaeuser (\$US)	36.17	3.74	4,483	14.13	26,499	9.7X	2.6X	5.9X
AVERAGE						16.0X	2.3X	6.5X

* Corton Capital Estimates

What did we find?

- **Price to Earnings (P/E) ratio for the Forest Sector is low** - The current S&P 500 P/E Ratio is 34.6x, while the P/E ratio for the primary wood product companies in the Timber Fund range from 1.8X (Interfor) to 9.7x (Weyerhaeuser). It should be noted that companies with substantial timber holdings such as **Rayonier**, **Weyerhaeuser** and **PotlatchDeltic** have higher P/Es due the underlying value of their timberlands. Two other pure timber holdings in the Fund are trading at higher P/E multiples namely **CatchMark Timber** (24.5x) and **Acadian Timber** (11.8x). **Traditionally, paper and forest stocks trade at a P/E multiple of 10x.**
- **Price to Bookvalue per share (BVPS)** – Price to BV has been long regarded as a reliable measure of how undervalued a company's stock price is. As illustrated in Table 1, several of the Canadian companies in the Timber Fund are actually trading at a discount to BV namely; **Canfor**, **Canfor Pulp**, and **Interfor**. A recent example of a more realistic BVPS multiple was the US\$3.1 billion acquisition of Norbord by West Fraser which was done at a **3.0x multiple of BV.**
- **Enterprise Value to EBITDa multiple** – Enterprise Value (as defined as market capitalization + debt – cash) is a good measure of the net worth of a company, however, when companies have substantial surplus earnings they tend to pay down debt and grow cash reserves. This reduces the EV and makes an EV/EBITDa multiple less relevant for valuation purposes. Typically, Paper & Forest Products companies have a EV/EBITDa trading range of 6.0-8.0x. As illustrated in Table 1, most of the companies in the Timber Fund are trading well below this range.
- **Other valuation methods** – There are two other primary valuation methods, **precedent transactions** and **replacement costs**. With regard to precedent transactions, as we mentioned above, the West Fraser/Norbord acquisition was done at a 3.0x multiple of BV. According to West Fraser and confirmed by recent greenfield sawmill announcements, the cost of a new sawmill in the U.S. is valued in a range of US\$550-\$650 per mfbm of annual capacity. When we applied these values to a simple Net Asset Valuation (NAV) model for some of the holdings in the Timber Fund, we found the companies were trading at a significant (50%+) discount to their underlying NAV.

Bottom Line – No matter what valuation technique we use, **all of the companies in the Corton Global Timber Fund are trading at a price with a substantial discount to their underlying value – range 27% - 134% with a weighted average of 72%.**

For more information on how to invest in the Corton Global Timber Fund, please contact: David Jarvis – David@cortoncapital.ca, John Duncanson - john@cortoncapital.ca, or Jenny O'Meara – jenny@cortoncapital.ca

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