



## **Barrons Asia - TFS Set to Harvest Growth In China and India**

There are not many companies - if any - that could capture an 80% market share of their industry. But that's the reward that Australian sandalwood grower TFS (TFC.AU) is eyeing as its investment in new supplies of the fragrant timber and oil are set to pay off as production ramps up to meet strongly growing Chinese demand.

CEO Frank Wilson, who owns a 12% stake in TFS, laughs off suggestions he's running the OPEC of sandalwood when he sat down with Barron's Asia, but he's acknowledges the company is in a strong position as its transitions from being a forestry investment play to a provider of products hotly demanded for use in incense, perfumes and traditional Chinese medicine.

The company has around 30% market share now, but as its plantations mature - trees take 15 years to grow - it could emerge with an 80% market share by 2030. The stock has done well over the past 12 months, with a 37% increase bringing its advance over the past five year to 140%.

TFS is the lone survivor of the shakeout of the Australian timber industry, one that saw a large number of forestry managed investment schemes (MIS) collapse under the weight of too much debt, leaving thousands of investors nursing heavy losses. For Wilson, the ability of TFS to survive the travails of the MIS debacle reflects a focus on a niche part of the industry, rather than more commodity type plantations favored by those forestry plays that hit the wall. "The reason I went into it is that it has big barriers to entry and it had a good end market that wasn't aimed at one particular manufacturer, industry or country, and that should eliminate the boom-bust cycle you have in agriculture," Wilson says. "That's proved to be true."

TFS, which as a market cap of AUD600 million, owns 12,000 hectares of sandalwood plantations across Australia. About half of its production is sold to China, where there is strong demand for use in traditional Chinese medicine. The company has a five-year contract to supply 150 tonnes a year to Chinese buyers. Other big buyers include U.K.-based Lush Cosmetics and U.S.-based Young Living. But it's the growth in the Chinese and Indian markets that Wilson is most excited about over the long term, especially given forecasts that global demand could grow to 20,000 tonnes by 2025. "We think there's always going to be a compelling supply-demand imbalance in our favor to support prices. It's the one area of our business that I don't have any concerns about – it's just the size of the Chinese and Indian market".

The forward selling of the bulk of harvests out until 2021 means that revenues are locked in. Those contracts will see the demands of existing clients met, but it leaves enough free supply to provide to new clients in the hope they will then sign on for more as TFS works up to a sustainable annual production of between 10,000 tonnes and 12,000 tonnes a year. "It's about balance between having enough travel in the system to feed new customers but having enough locked in to make everyone feel comfortable and certain you've got a market". The company has forecast a 25% increase in its cash EBITDA (earnings before interest, tax, depreciation and amortization) in the 2017 financial year, which ends on June 30.

One strongly growing area of demand for sandalwood products is pharmaceuticals. TFS' Santalis business is developing drugs aimed at alleviating eczema and psoriasis – there are four drugs in phase two trials with the U.S. Food and Drug Administration. Wilson sees the Santalis business as a bit of a hidden gem with the TFS business, and believes a sale of a stake in the business of an IPO could help realize its value. "At the moment you have this agribusiness company with a pharmaceutical subsidiary stuck in there. If we can shift it out so it has its own spotlight that can have a valuation that can equal the current valuation of TFS pretty quickly."

Source: <http://www.tfsltd.com.au/blog/barrons-asia-tfs-set-harvest-growth-china-and-india/>

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