

Growing Trends

NEWSLETTER FOR GROWERS AND SHAREHOLDERS

June 2011

TRIAL INDIAN SANDALWOOD HARVEST PRODUCES HIGH QUALITY COMMERCIAL OIL YIELD RESULTS

Final results from an investigation of age 19-23 Indian Sandalwood trees have provided promising results which support TFS's long term yield predictions.

A trial harvest was conducted by TFS and the Forest Products Commission Australia (FPC) on 90 trees from four FPC trial plots within the Ord River Irrigation Area. Results have shown that the trees have returned both high quality oil and high quantities of oil.

Key results have found that trees have yielded a mean of 25kg of Heartwood per tree, and 4.9% w/w mean oil from the Heartwood. The findings from the trial have also revealed the mean amount of oil yield per tree was 1.2kg, 50% higher than TFS's prediction of 0.8kg at age 15. The trial also showed that the oil fell within the ISO specification for high grade album oil suitable for fine fragrance industries.



TFS believes that constantly improving silviculture practices, such as host selection and genetics, will produce trees on average superior in size and yield to those of the harvested trees.

Executive Chairman Frank Wilson said "These are very encouraging results. For the first time a significant sample of mature trees has been harvested and subjected to destructive testing. The results support our yield predictions and indeed substantiate the core metrics of our investment model."

The trial was subject to a full independent audit by the University of Western Australia. Full production results are available on the TFS website – www.tfsltd.com.au.



OIL PRICE UPDATE

On the 19th May 2011, the Indian Sandalwood oil price as quoted by the UK Public Ledger and referenced through the Thomson Reuters Datastream database, increased from US\$2,125 per kg to US\$2,300 per kg.

Last June the price for Indian Sandalwood oil was US\$1,800 per kg, resulting in a price increase of 27.7% over the last year.

TOP PERFORMER



Mario DiLallo is the Head of Global Product Sales having joined TFS in 2007. Under Mario's stewardship Mount Romance Australia (MRA) sandalwood oil sales have reached record levels as MRA increases its presence in the Indian and Middle East markets. Mario was instrumental in shifting the focus of our sales efforts from Europe to India.

SANDALWOOD MAKES SCENTS IN BROOME

TFS has launched its new Mount Romance Sandalwood Gallery in Broome.

The Sandalwood Gallery is the third retail outlet for Mount Romance, following the success of the Kununnurra and Albany showrooms.

The Sandalwood Gallery opened its Carnarvon Street doors in early May to stock Mount Romance beauty and lifestyle products and to showcase Sandalwood as an ancient resource and one of WA's oldest industries.

"Our aim is to create a store that keeps tourists interested but also offers locals good quality, good value products," said Peter Wilson, General Manager of Mount Romance.

The world-class showroom has served to reinforce the already strong commitment between TFS and the Kimberley region.

The Kimberley region is home to the world's largest Indian Sandalwood plantation managed by TFS, and its Kununnurra showroom has been met with success.

"We see the roll out of The Sandalwood Gallery in Broome as an important part of our Kimberley presence and significant in light of the region's Sandalwood industry," said Frank Wilson, Executive Chairman of TFS.



Corporate Snapshot

TFS Corporation Ltd (TFS) (ASX Code: TFC) has continued to diversify its business model through FY11 amidst continued fall-out from the last of the main independent MIS companies, Willmott Forests to enter into Voluntary Administration.

The key feature of FY11 to date has been the settlement of the first two transactions in TFS's wholesale investment business. In September 2010, TFS settled a transaction with a AAA rated US investor that is a leader in global forestry investment. The transaction was a deal to plant 182ha with an option to plant a similar amount each year over the following five years. The transaction reflected a \$20m investment over the life of the project generating cash flows through the project. This investment was concluded after a long period of due diligence by the US investor. In a positive development, in December 2010, the US investor exercised their first option to invest in plantings of another 182ha in FY11. This second investment is based on similar terms to the initial transaction.

The second institutional investment transaction was settled in January 2011. This was a 376ha transaction with a Middle East Sovereign Wealth Fund (SWF). This transaction resulted in the payment of \$27m in up-front fees and a further \$13m in ongoing fees through the life of the investment. This transaction also includes a five year option.

The settlement of this transaction concludes a key development for TFS and reinforces the success of TFS's initiative to develop an institutional investment product for the wholesale market. The settlement of this transaction, along with two rounds of investment from the AAA rated US investor, provides a strong foundation for the success of this new business segment and global recognition of the sound fundamentals underpinning TFS's Indian Sandalwood business.

One of the key benefits of this new product line is that the timing of the receipt of funds should in general now be aligned with the sales and planting cycle, such that the strength of the underlying cash flows will become transparent.

TFS has a very strong pipeline of institutional investor interest which forms the back drop to TFS's recent FY11 forecast of circa \$70m at the Operating Cash Flow line.

The settlement of the transaction with the SWF combined with a \$37.9m equity raising to facilitate paying out TFS's debt with the CBA.

In other news, TFS recently received its product ruling from the ATO for a new MIS Indian Sandalwood project in 2011. This is the 13th successive project that TFS has launched. The 2011 project is offering up to 3,000 woodlots of one sixth

of a hectare (500ha) with capacity for oversubscriptions. TFS has received a 4 & ¼ star rating from independent research house Adviser Edge, which is the highest ever rating awarded to a TFS project by Adviser Edge. TFS is expecting an improved outcome this year in the face of significantly reduced competition in the MIS sector.

One of the pleasing developments in the recent half year results was the strong cash flows in the MRA processing and distillation business. Operating cash flow was +\$11m and well ahead of EBITDA of \$1.7m. This reflected strong collections as well as a new order where payment was received in advance of delivery. This suggests that supply conditions continue to tighten providing favourable outcomes for TFS. Approximately 70% of MRA's production over the next three years is now sold with prices expected to rise over the balance in the near term.

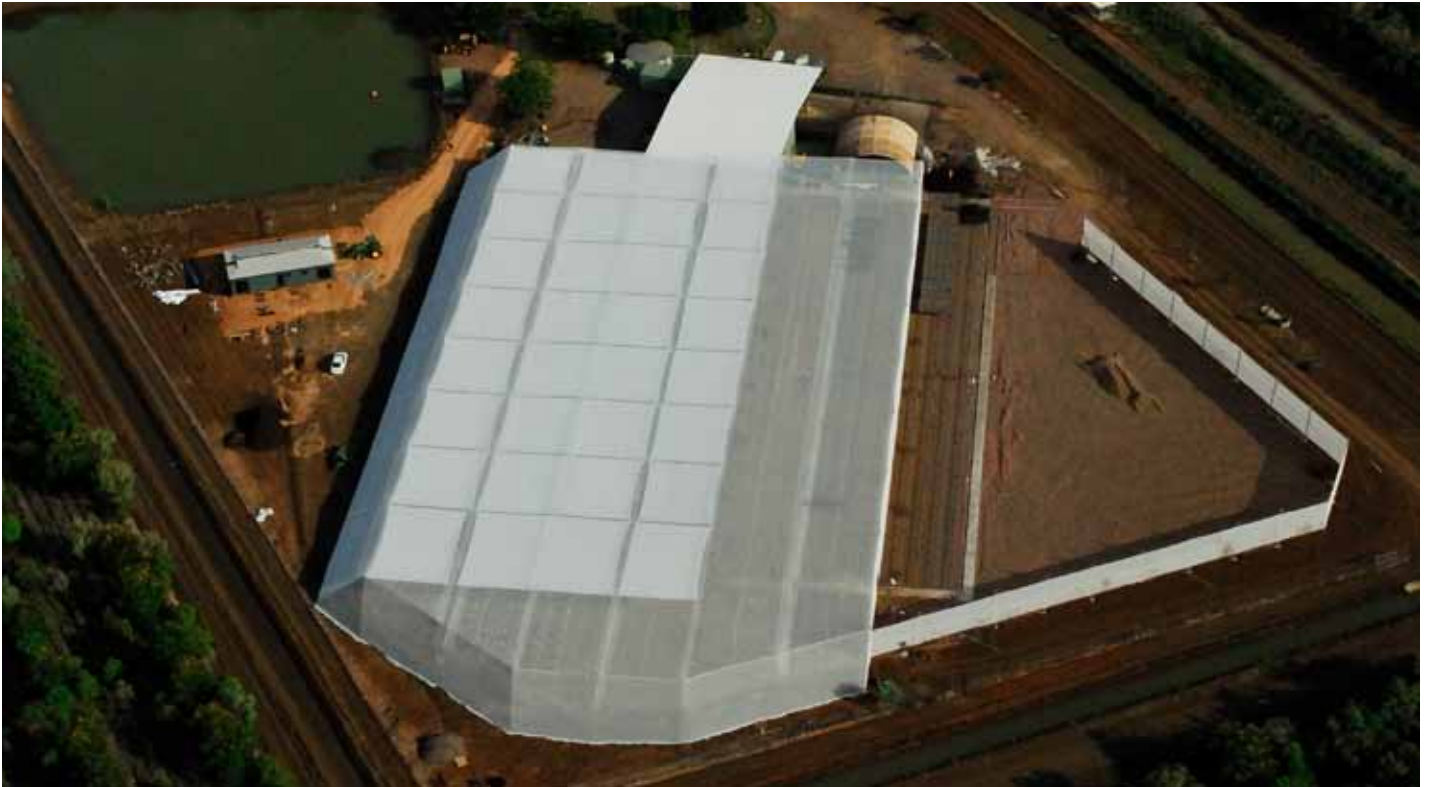
The MRA result contributed to the improved cash flow performance at the half year. In conjunction with the settlement of the institutional investor transaction in January, Operating Cash Flow experienced a positive \$44m turnaround for the seven months to January 2011, where operating cash flow was +\$23m.

At the half year result, TFS re-stated its full year guidance of growth in cash earnings of at least 10%. By June, TFS will have completed a significant year in its development with a consolidation of the wholesale product and new funding enabling the business to fulfil its ambition of being a global leader in the Sandalwood industry.

FY11 will prove to be a momentous year in TFS's development.



Plantation Report



TFS HAS THE LARGEST PURPOSE BUILT INDIAN SANDALWOOD NURSERY IN THE WORLD, WHICH HAS THE CAPACITY TO PRODUCE OVER HALF A MILLIOIN SEEDLINGS PER PLANTING SEASON.

The TFS Indian Sandalwood plantation estate at Kununurra continues to expand, with an additional 1,200ha to be planted during 2011. This will take the total estate to almost 5,000ha. The majority of the plantations are located within the Ord River Irrigation Area, with the balance at Kingston Rest.

Kingston Rest is a property owned by TFS that is located approximately 75km from Kununurra. It has an on-farm 65GL dam, which supports an independent irrigation system. Over the past few years TFS has converted the property from a semi-developed flood irrigated hay farm into a fully developed 1,450ha sandalwood plantation, with an industry leading pressurised irrigation system.

The 2010 / 2011 wet season was one of the wettest on record, with heavy and prolonged rainfall right through to the middle of April. Total rainfall for the wet season was over 1,400mm, which is well above the 800mm long term average. Plantation operations ceased due to lack of access during this time. Sandalwood can not tolerate long periods of inundation or flooding, and hence well designed and maintained drainage systems are imperative to ensure that water is quickly removed from the paddocks.

TFS is pleased to report that all on-farm drainage systems worked efficiently during the extremely wet conditions, and that the sandalwood plantations have not suffered any material adverse health impacts due to the prolonged wet weather, although there was some damage to a small area of the Packsaddle plantation.

Post wet season plantation maintenance commenced across the estate in late April, when conditions became dry enough for ground based operations. The main activities being undertaken are weed control and form pruning of the sandalwood, as well as routine maintenance of irrigation infrastructure and fire breaks.

The research division in Kununurra continues to provide valuable information to TFS. Growth and yield models for heartwood and oil production have been developed using a combination of in-field inventory methods as well as trial harvest results. The research division is also developing a genetic improvement (tree breeding) program through the establishment of seed orchards. Selection of parent trees for the seed orchards is based on their superior growth and superior oil yield. Seed produced from these orchards will improve the quality of future plantations.

TFS SANDALWOOD PROJECT 2011

Despite the demise of many of the players in the Agribusiness sector over the past 2 years, TFS has launched its 2011 Indian Sandalwood Project, reflecting its commitment to the MIS sector. The ATO has issued a Product Ruling which confirms 100% tax deductibility of the establishment fee and the annual management fees in the years that they are paid.

AdviserEdge Research has awarded the project with 4 ¼ Stars, largely in recognition of the quality of the project we are offering but also acknowledgement that we have “weathered the storm” and now emerged as a financially sound company with substantial upside over the coming couple of years as we move towards our first commercial harvest of Indian Sandalwood in fiscal year 2012/13. This will be another watershed milestone for the company.

It is refreshing to see that TFS has not varied from its core strategy of becoming the largest and best vertically integrated Sandalwood company in the world. Unlike so many of our failed competitors, we have continued to pursue that vision and not headed off on a tangent to pursue other projects that appeared to be more attractive but at the same time, can be financially draining.

TFS has withstood the test of time and has emerged as a stronger and financially sound enterprise and proudly able to boast that our grower's investments are secure. Some of the highlights of the past 12 months are:

- TFS has repaid all bank loans in full.
- AAA Rated US Institution settles the first 180ha tree plantation transaction worth c\$20million to TFS.
- The same AAA Rated US Institution exercised its first annual option.
- In January 2011 a Middle Eastern Sovereign Wealth Fund settled a \$47million investment in plantations to be managed by TFS and has a further 4 annual options.
- TFS enters into a JV with San Antonio based pharmaceutical company, Viroxis, to develop topical



ointments to treat several skin disorders, thus creating further previously untapped use for Sandalwood oil and other products.

- TFS's financial viability is now less than 20% reliant on income from MIS Sales.
- Results from the analysis of Indian Sandalwood trees grown in Kununurra support the assumptions that we made about yields in our PDS.
- With the investments being made by the two institutions detailed above, we have seen the genesis of a secondary market for TFS Indian Sandalwood Trees. Therefore investments in our projects become liquid after the expiration of just 4 years, in line with recent changes to Taxation Laws.

The 2011 Project is in most respects similar to the 2010 Project with the exception that the Establishment fees have been increased marginally to \$12,500 (plus GST) for 1-5 woodlots and to \$12,000 (plus GST) for 6 woodlots or more. As a result of TFS now achieving economies of scale in its management regime, annual management fees have been reduced to compensate for the slightly higher establishment fees. In the knowledge of survival rates we are achieving in our plantations and the analysis of the trees referred to above, TFS has again set the stretch target for Net Proceeds

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of Sale at \$200,000 per woodlot meaning that we will not be entitled to a Managers Performance Bonus until such time as we have returned a minimum of \$200,000 per woodlot to growers.

Woodlots can be acquired using the 12 months interest free loans being offered by Arwon Finance Pty Ltd which are based on a deposit of 20% being paid at the time of application with the balance being paid by 12 equal monthly installments.

The need for investments in a high quality Agribusiness project is still very real. With the rules for Superannuation now limiting the maximum amount that any one person can contribute into superannuation, Agribusiness is the most

efficient way of being able to set aside income/wealth for the future, and on a tax effective basis.

TFS has come through the global financial crisis as a well credentialed and financially sound company with a single focus. We continue to be able to offer clients a product that can support the concept of diversification of their investment portfolios.

The Product Disclosure Statement (PDS), Product Ruling and other material is available for viewing and downloading at our website. Investors looking to make an investment in this most exciting project should read the PDS entirely and also consult with their regular financial adviser.

KEEP UP-TO-DATE ONLINE

The TFS website - www.tfsltd.com.au is an informative website designed for growers, shareholders, advisers, buyers and potential investors. Updated information on TFS news, company policies and forms, current offerings, annual reports, project accounts and general sandalwood information can be easily located.

If you have any suggestions or comments on the site please feel free to contact us at tfs@tfsltd.com.au.

PROJECT FINANCIAL REPORTS - Project Financial Reports for the financial year ended 30 June 2010 are available for growers to view and download from the MIS INVESTOR section of our website.

Like all environmentally aware businesses, TFS is continually striving to minimise the impact of its operations on the environment and reducing the physical quantity of paper that it uses is one way that it is able to shrink its overall carbon footprint and make a contribution to minimising climate change. Electronic copies of the Annual Reports are available from our website and growers can, if they wish, save a copy onto their own computer facilities as a permanent personal record. Alternatively, if you would like to receive a hard copy of the Annual Report, please email your request to tfs@tfsltd.com.au.



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