



Timberrrrr!

Description

Rarely has the phrase “trees don’t grow to the sky” been more applicable than describing the current state of stocks in the Canadian forestry sector. After years of neglect and misery, forestry stocks have been hot. Really hot. And as the following charts show, potentially too hot.

Have a look at where the current price/book multiple stands in relation to history for three of Canada's biggest forestry companies, **West Fraser Timber** (TSX:WFT), **Canfor** ([TSX:CFP](#)), and **Interfor** (TSX:IFP.A).

[WFT Hist PB](#)
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West Fraser, Canfor, and Interfor are up 105%, 94%, and 125% respectively since the beginning of 2012 on the back of lumber’s 55% move over the same period. As these charts demonstrate, company fundamentals have not supported this move as book value has remained relatively stable.

What’s next?

There are a couple of ways for these stocks to move higher from here:

1. The multiple can continue to expand or at least remain static as book value grows.
2. Book value can go up faster than the multiple comes down.

Given the all-time high multiples, further expansion or even maintaining the current level is a low probability event.

And, if we assume the multiples revert to their mean over time, the book value growth required to maintain the current share price is astronomical relative to historical growth rates. The following table outlines this scenario:

Company	Current P/B	Historic Avg	Reversion	Current BVPS	Req'd Growth
West Fraser	2.6	1.1	-57.7%	\$34.81	132.9%
Canfor	2.8	1.0	-64.3%	\$7.78	172.5%
Interfor	1.5	0.7	-53.3%	\$6.73	118.6%

Source: Capital IQ

Just to be clear, the required growth in book value per share (second last column) required to offset the potential mean reversion that the multiples face is way (waaaaaaay!) beyond the book value growth that these companies have been capable of in the past (last column).

The Foolish Bottom Line

Long-time holders of these stocks have finally had their patience pay off with the rally that has occurred but should now be taking a long hard look at the scenarios required for this run to continue. It's a stretch to believe book value growth will eclipse multiple erosion over an extended period. Management at each company warrants a pat on the back for surviving the U.S. housing downturn and even bolstering their respective companies for the rebound that has begun to play out. The stocks however appear to have moved well ahead of the fundamentals. It might be time to bring out the axe and hack these names out of your portfolio.

Forestry was a beaten down resource for many years that is now surging. We have created a special report that outlines another neglected resource that is poised to experience a similar resurgence. Simply [click here](#) and we'll send you the report, absolutely free!

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Fool contributor Iain Butler does not own shares in any of the companies mentioned in this report at this time. The Motley Fool has no positions in the stocks mentioned above.

CATEGORY

- Investing

TICKERS GLOBAL

- TSX:CFP (Canfor Corporation)
- TSX:WFG (West Fraser Timber Co. Ltd.)

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