

Timber - A High Yield Asset That Never Stops Growing

Who says that money doesn't grow on trees? Did you know that timber was one of the ONLY assets that appreciated in 2008? Just take a look at the high yield stocks in the diversified timber REIT sub-industry, and you might just might launch into a verse of Monty Python's "Lumberjack Song"...

One Timber Reit that comes up in a screen for high dividend yields is Potlatch Corp., (PCH). A metric that investors use when analyzing timber companies is the amount of acres/share. At Potlatch's current price of \$26.77, you get approximately 38-39 acres/share, plus you get the rest of the business for free, (land sales & development, and wood products manufacturing).

Potlatch recently announced a cutback in timber harvesting, due to soft market prices, but is maintaining their dividend of \$.51/share/quarter, for a 7.62% yield.

You can juice PCH's high dividend yield even further, by selling January 2010 covered calls, essentially earning an extra, or "double dividend". Please note that each call contract controls 100 shares of the underlying stock.

Here's how it would work, based upon 100 shares.:

1. Buy 100 shares PCH at \$26.77
2. Sell 1 Jan 2010 \$30 call for \$2.20
3. Collect \$1.53 in dividends, (\$.51/share for the final 3 quarters of 2009)
4. At Jan. 2010 expiration, one of two things will happen:

Scenario A - Assignment: If PCH's price rises to or past \$32.20, your 100 shares will be sold/assigned at \$30.00, giving you a capital gain of \$3.23/share, in addition to the \$3.73/share call premium and dividend income you received.

OR

Scenario B - Static Return: If PCH doesn't rise to or past \$32.20, (which equals the strike price plus the call premium of \$2.20), you keep your 100 shares, and walk away with the \$3.53/share income, which lowers your basis to \$23.24. At this point you could repeat the process again, if prudent.

The details for this 8-month trade are:

Breakeven: \$23.24/share

Upside Trigger Price: \$32.20

Static Call Yield: 8.21% Call Premium: \$220.00

Dividend Yield: 5.72% Dividends Paid: \$153.00

Total Static Yield (Call + Dividends): 13.93% or 20.95% annualized

Potential Assigned Yield: 13.93% \$373.00 on sale at \$30.00

Total Potential Assigned Yield (Total Static + Cap. Gain): 27.87%

The 8-month 27.87% yield equals an annualized yield of 41.8%

So, we started out with a high dividend stock yielding 7.62 %, then we locked in an additional 8.21%, (12.3% annualized), plus we set ourselves up for a total potential annualized yield of 41.8%.

In addition to juicing your yield, this strategy also lowers your breakeven considerably, giving you 13.93% downside protection. One other benefit to this strategy is that you know exactly what your upside potential profit is.

It's enough to make you yell "Timber!"