# Should You Buy Labrador Iron Ore Royalty Company?

## Description

In *Canadian Business Magazine*'s newest issue, they reveal the five "hottest stocks to buy right now". Four of them had total returns greater than 40% last year, which may mean the best time to buy them has already passed. But one stood out, perhaps because it returned only 2.6% in 2013: **Labrador Iron Ore Royalty Corporation** (TSX:LIF). The company has been the subject of fierce debates, activist investors, and takeover rumours in the past year.

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LIORC's revenues and earnings come entirely from the Iron Ore Company of Canada (IOC), which mines iron ore from the Labrador trough. LIORC owns a 15.1% stake in the IOC, but also owns a 7% royalty on IOC's sales.

Last year Waratah Advisors, a Toronto-based activist hedge fund, made the case that LIORC should pursue various "strategic alternatives", including selling its 15.1% stake in the IOC. The argument was that LIORC was undervalued due to its confusing structure – divesting the equity stake in the IOC would allow the royalty piece to trade on its own merits. Royalty companies at the time had extremely rich valuations, and Waratah was arguing that LIORC's royalty would be no different.

Canada's largest royalty companies are **Franco Nevada** (TSX:FNV) and **Silver Wheaton** (TSX:SLW). The two companies sign royalty deals in gold and silver respectively. They have given investors an excellent way to gain exposure to precious metals and thus trade at very high multiples.

These high multiples are understandable. There are many investors who are afraid for the world economy, want to diversify their portfolio, or who simply want some exposure to precious metals. Franco and Silver Wheaton offer that opportunity without the risk of seeing dramatic cost over-runs, which have come far too frequently from the miners themselves.

But how many people are demanding a royalty for iron ore? Unlike precious metals, iron ore is very dependent on the health of the economy. Concerns about a property bubble in China affect steel and iron ore more than any other major commodity. A bet on iron ore does not provide the kind of diversification that precious metals do.

Making matters worse, the major iron ore players have been planning $250 billion worth of mine expansions, threatening to create a serious supply glut. Well-known hedge fund manager David Einhorn established a short position in iron ore in late 2012, referring to the commodity as a “bubble”.

This all makes LIORC a very interesting pick for Canadian Business’s hotlist. Perhaps LIORC’s 5.9% dividend yield plays a part. But as any investor knows, it is impossible to get a 5.9% yield without taking some noticeable risk.

**CATEGORY**

1. Investing

**TICKERS GLOBAL**

1. NYSE:FNV (Franco-Nevada)
2. TSX:FNV (Franco-Nevada)
3. TSX:LIF (Labrador Iron Ore Royalty Corporation)
4. TSX:WPM (Wheaton Precious Metals Corp.)

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