3 Top Stocks With Wide Economic Moats for 2016 and Beyond

Description

An important aspect of successful investing is identifying companies that possess wide and almost unassailable economic moats.

An economic moat is the ability of a company to maintain its competitive advantage over its competitors, thereby protecting its earnings growth. The importance of a solid economic moat can't be stressed enough as it virtually guarantees a company's earnings growth over time.

The one company that has the most widely recognized and probably the strongest economic moat around is **The Coca-Cola Co** (NYSE:KO). Not only does it have over 3,000 products that are distributed worldwide, but its brand and market share have proven almost unassailable. It is one of the most iconic products of all time.

Let's take a closer look at three Canadian companies that possess solid economic moats.

Now what?

The first company is Canada's largest rail network **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI). It operates Canada's only transcontinental rail network, giving it and Canada's other major rail company **Canadian Pacific Railway Limited** a virtual duopoly on Canada's rail traffic.

The steep barriers to entry in what is a heavily regulated and capital-intensive industry shield Canadian National from competition. This, along with the oligopolistic nature of Canada's rail industry and the fact that rail will remain the dominant form of bulk transportation, protects Canadian National's future earnings.

It is also worth noting that Canadian National has a lower dependence on bulk transportation of coal and other commodities than many of its North American peers. This means that the impact of weak commodity prices on its revenues will be minimal.

Another Canadian stock with a solid economic moat is **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS).

The heavily regulated nature of Canada’s banking industry essentially protects the incumbents from competition. Then you have to consider that between them, the big five control the majority of Canada’s banking and wealth management market, making it difficult for any credible competition to emerge.

Bank of Nova Scotia is the best pick because unlike **Toronto Dominion Bank** or **Bank of Montreal,** it has avoided the fiercely competitive U.S. banking market and has chosen to expand in the rapidly growing markets of Latin America.

While there are certainly risks with this strategy, the bank has diversified its operations across Mexico, Colombia, Peru, and Chile, thereby minimizing those risks. These markets are also under banked and have rapidly growing middle classes, providing significant growth opportunities.

The final pick is electric utility **Fortis Inc.** (TSX:FTS).

Significant regulatory barriers coupled with the capital-intensive nature of the industry provides electric utilities, and the inelastic demand for electricity endows it with a solid economic moat. This protects Fortis’s future earnings and virtually guarantees that earnings will grow as demand for electricity rises.

Then you have to consider the diversified nature of Fortis’s operations. It operates in the U.S. and Caribbean as well as Canada. This also helps to protect its earnings by minimizing the impact of any localized economic downturn.

In fact, with almost 72% of its net earnings coming from the U.S., I would expect a nice bump in Fortis’s bottom line because of a strong U.S. dollar and a growing U.S. economy.

So what?

The solid economic moat possessed by each of these companies allows them to sustain strong profit margins, which gives them the capacity to earn excess profits and deliver sizable returns on invested capital, thereby unlocking considerable value for investors over the long term. This makes each stock a core, long-term holding for any portfolio.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:BNS (The Bank of Nova Scotia)
2. NYSE:CNI (Canadian National Railway Company)
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