



Is Brookfield Asset Management Inc. the Perfect Forever Stock?

Description

A good forever stock has the following attributes:

- A business with loads of potential growth
- A business that delivers consistent profits with good margins
- Easy to understand
- The ability to reinvest earnings at attractive rates of returns
- A sharp management team running the show
- Trades at a reasonable valuation

There's a reason why those characteristics sound a lot like what Warren Buffett looks for in a company. I, like many other investors, have borrowed heavily from the Oracle of Omaha. It's obvious his equation works. Why would I mess with it?

Most Canadian companies meet a few of these criteria. Many of Canada's largest companies are run by smart people and deliver great margins. But they're so mature that there's little potential to reinvest profits back into the business to really goose growth. They just get paid to shareholders.

There are only a select few companies that meet all the different criteria of a business investors want to own for the rest of their lives. Here's why **Brookfield Asset Management Inc.** (TSX:BAM.A)([NYSE:BAM](#)) is one of those stocks.

Unlimited growth potential

Brookfield's business model is as simple as it is powerful. It manages all sorts of assets for institutional clients.

Here's how it works.

The company recognizes an opportunity in a sector, say real estate. It puts some of its capital into an investment entity and then attracts additional capital from pension funds, sovereign wealth funds, rich folks, and the like. It uses this seed capital to launch a vehicle dedicated to acquiring and managing

assets.

The company gets paid to manage these assets, of course. Some of these earnings are paid back to shareholders—the current yield on Brookfield Asset Management’s shares is currently 1.7%—but most of the earnings from management fees are ploughed back into the businesses.

The strategy seems to be working. Brookfield currently manages more than \$225 billion worth of assets in its many subsidiaries. Sectors of interest include commercial and residential real estate, infrastructure, renewable energy, and private equity.

Approximately 45% of revenue comes from the company’s publicly listed partnerships with 35% coming from management fees on private funds. The rest comes from a combination of public markets and transaction/advisory services.

It’s easy to see the growth potential in this model. As more and more assets migrate to the ultra-wealthy, these people will seek managers like Brookfield to get a decent return on the capital. It’s worked pretty well so far; including reinvested dividends, shares of the company are up nearly 21% annualized over the last 15 years.

Good profits

The beauty of the asset management business is that it has great margins.

Let’s look at the past quarter as an example. Brookfield had revenue of US\$5.5 billion, an increase of nearly 20% compared to US\$4.7 billion in revenue during the same quarter last year. Operating income was US\$1.4 billion, giving the company operating margins of more than 25%.

Those are the types of profit margins any investor can get excited about.

Reasonable valuation

Buying good businesses is only half the battle. Investors also must make sure they get these stocks at a reasonable valuation.

Brookfield is a little tricky to value. The company has many moving parts, assets that can be valued a number of different ways depending on things like discount rates. There are accounting principles that do influence the value of the underlying assets, but they’re more general rules. There’s definitely some wiggle room there.

Here’s how I like to value Brookfield.

It has approximately \$28 billion of its own capital invested in its various vehicles. The company has a market value of \$41.4 billion. That means investors are paying \$13 billion for a business that manages almost \$100 billion in external capital.

Or, to put it another way, Brookfield delivered \$2.49 per share in funds from operations in 2015. Investors buying today are picking up shares for 17 times that metric, a reasonable valuation.

There's a lot to like about Brookfield Asset Management. Perhaps investors should look at making the company a permanent fixture in their portfolios.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:BN (Brookfield Corporation)
2. TSX:BN (Brookfield)

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