



If You Own 1 Gold Stock, Make it Franco-Nevada Corp.

Description

Allow me to start this with a bit of a confession. I don't really like the gold sector.

There are several reasons for my hard feelings. Commodities are a tough business to be in when times are difficult. There's no way for a gold, oil, or copper producer to add any value to their product. Gold is gold, whether it comes from Russia or Canada or the moon.

I take that back. Moon gold would be cool enough to demand a premium.

Additionally, I've never really been one to believe our whole monetary system is about to collapse, turning the \$20 bills in my wallet into worthless pieces of paper. Fiat currency works pretty well. Sure, you can point at countries like Venezuela currently or Zimbabwe a few years ago as situations where the concept went terribly wrong, but for the most part, it works. Besides, owning other assets like real estate helps hedge inflation.

And then there's the business itself. Every gold company comes with two sets of risks: the price of the commodity, which is completely out of a producer's hands, and operational risk, which is something a gold miner can control. Many companies in the sector have long histories of struggling to keep costs low and construction projects on schedule.

It's for these reasons why I've avoided the sector throughout my investing career. I've always found there to be too many interesting businesses available for investment to really dig into the precious metals sector.

After saying all that, there is one gold company that does interest me today. What makes this company unique is it takes on almost zero operational risk, while its entire business model minimizes commodity price risk.

That company is **Franco-Nevada Corp.** ([TSX:FNV](#))([NYSE:FNV](#)). Here's why even non-gold bugs like me should at least consider owning it.

The lucrative streaming business

Viewers of the hit CBC television show *Dragon's Den* likely remember Kevin O'Leary's numerous requests for pitchers to give him a royalty stream as part of his offers.

Maybe Franco-Nevada execs were inspired by O'Leary, because its business model is essentially royalties off gold mines.

Here's how it works.

A gold (or silver) producer approaches the company with a problem. It has what appears to be a promising mine, but no cash to develop it. Franco-Nevada agrees to supply that cash in exchange for buying a portion of future production at a huge discount.

Let's take a look at the company's latest streaming deal. It paid US\$500 million to Glencore for the right to receive approximately 70,000-80,000 gold equivalent ounces annually until production runs out at the Antapaccay mine in Peru, which is slated to be around 2030.

Even if gold prices don't rise significantly, this still looks to be a pretty good deal for Franco-Nevada. Assuming just a US\$1,000 per ounce price for gold, the deal is still profitable. If gold shoots up to \$1,500 per ounce, shareholders will be very happy.

That's the beauty of Franco-Nevada's business model. Even if gold stays around where it's at today, the company is still poised to make a decent return on its money. But if gold heads higher, shareholders keep all that upside. Thus, Franco-Nevada gives investors exposure to higher gold prices while still protecting them on the downside.

That's an incredibly powerful business model, and it shows up when we look at the stock's performance over the last five years. Shares of Franco-Nevada are up 124% since 2011, absolutely trouncing Canada's largest gold ETF, the **iShares S&P TSX Global Gold Index Fund**, which lost nearly 45% during the same period.

Plus, Franco-Nevada pays a modest dividend, coming in at 1.4%. Sure, that doesn't seem like much when looking at other dividend stocks, but it's one of the only stocks in the sector that pays a consistently rising dividend.

Franco-Nevada isn't like other gold stocks, and that's a good thing. It's intriguing enough that even this staunch anti-gold bug is taking a good look at it. Perhaps you should too.

CATEGORY

1. Dividend Stocks
2. Investing
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TICKERS GLOBAL

1. NYSE:FNV (Franco-Nevada)
2. TSX:FNV (Franco-Nevada)

3. TSX:XGD (iShares S&P/TSX Global Gold Index ETF)

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