Porter & Co.

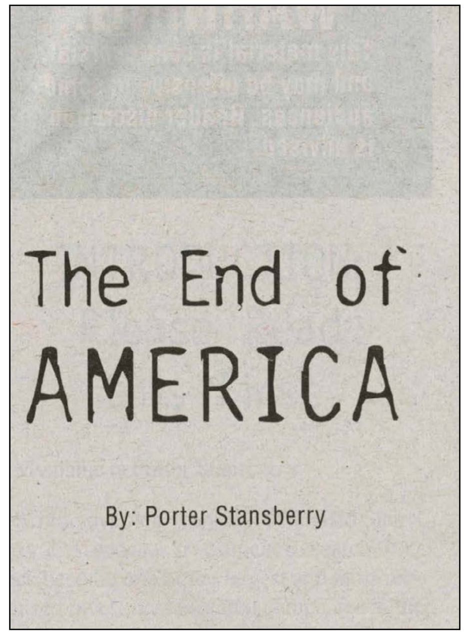
CRASH-PROOF EQUITIES

SIX COMPANIES TO PROTECT YOUR WEALTH

Crash-Proof Equities

Porter Stansberry's Next Big Prediction

Six Stocks to Guard Against The Upcoming Economic Collapse


The End of
AMERICA

By: Porter Stansberry

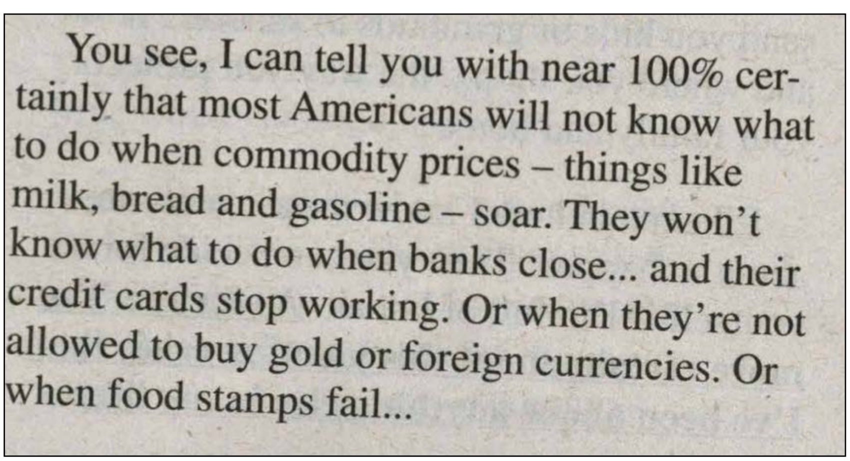
I've been making people angry for a long time.

My name is Porter Stansberry. I've been "canceled," blacklisted, and threatened more times than I can count... ever since, way back in 2011, I wrote a slim, 91-page booklet called THE END OF AMERICA.

Maybe you remember it. Maybe you even thumbed through a copy. Thousands were distributed across the country – winding up in gas stations, on kitchen tables, and in more than a few boardrooms and executive offices.

By then, I'd already made a name for myself in the investment research world by correctly predicting the collapse of Fannie Mae, Freddie Mac, General Motors, General Electric, and many other "too big to fail" companies. But the predictions I made in THE END OF AMERICA were different... and frightening.

I warned Americans that – as the U.S. monetary system collapsed under the weight of unsustainable debt – they could expect food shortages, soaring commodity prices, civic unrest, riots in the streets... and much more.


You see, I can tell you with near 100% certainty that most Americans will not know what to do when commodity prices – things like milk, bread and gasoline – soar. They won't know what to do when banks close... and their credit cards stop working. Or when they're not allowed to buy gold or foreign currencies. Or when food stamps fail...

> **In short, I want to detail for you a specific event** that will take place in America's very near future... which could actually bring our country and our way of life to a grinding halt.
>
> This looming crisis is related to the financial crisis of 2008... but it is infinitely more dangerous, as I'll explain in these pages.
>
> As this problem comes to a head, I expect there to be riots in the streets... arrests on an unprecedented scale... and martial law, enforced by the U.S. military.

> The savings of millions will be wiped out. This disaster will change your business and your work. It will dramatically affect your financial accounts, investments, and retirement.
>
> It will change everything about your normal way of life: Where you vacation... where you send you kids or grandkids to school... how and where you shop... the way you protect your family and home.
>
> I'll explain how I know these events are about to happen. Then you can decide for yourself if I'm full of hot air. **As for me, I'm more certain about this looming crisis than I've been about anything else in my life.**

Naturally, this wasn't a popular message. I caught plenty of flak for being too pessimistic and "un-American."

But I had done my research, and I knew:

- One of the many repeating themes of paper money is the inevitable decline of liquidity as bad money forces out good.
- As long as paper money continues getting added to our system, our government will continue to overreach... our society will continue to be plagued by massive income inequity and social unrest... and our economy will grow progressively less efficient.
- Sooner or later, the U.S.'s massive credit bubble will deflate and the paper-money currency that enabled it will collapse.

And in the 13 years since I published THE END OF AMERICA...as our debt bubble has begun to unwind... almost all of the predictions in that little book have come true.

You've watched the riots on television... you've seen the news of high-profile bank failures...you, or someone you know, have struggled to afford a house... and I'm guessing you've been to the grocery store lately and seen that a loaf of bread costs twice as much as it used to.

The End of America is a lot closer today than it was in 2011. But don't panic.

Back then, I offered two really simple recommendations for how to protect your money from the coming collapse – and, if anything, they're more relevant today. First, I recommended that readers diversify their assets out of the American monetary system – and second, that they buy a lot of precious metal.

So here are the specific steps you should take...

STEP #1. GET SOME OF YOUR MONEY BEYOND THE REACH OF THE U.S. GOVERNMENT (it's perfectly legal, and a lot easier than you think)

I know you probably don't believe me when I tell you that the U.S. government is going to

on...

STEP #2: HOW TO ACQUIRE THE WORLD'S SAFEST ASSETS, WHICH ARE LIKELY TO PERFORM BEST DURING THIS PERIOD.

What I'm talking about here is buying as much gold and silver as you can reasonably afford. I know... gold has had a huge run, jumping more than 300% in the past decade.

This is a big reason why I get along with Michael Gibson so well today. Michael is an expert on safely and legally getting your money out of the U.S., and on purchasing gold and silver – and if you visit his **website** or his **Instagram page**, you'll get a master's-level education on these techniques.

Of course, Michael and I don't see eye to eye on everything...

Michael hates stocks. I don't. In fact, I think certain stocks – ones I like to call "forever stocks" – can actually be a powerful additional tool to protect yourself from a catastrophic crash.

And while in Michael's perfect world, no one would own a single equity – he recognizes that's not realistic. Many of you still want to purchase stocks... and you need some guidance while doing so. So Michael's agreed to let me share a few of my favorite "forever stocks" with you. In his words, I'm one of the only "shepherds" he trusts to show you the way.

In my opinion, one of the *safest* places you can put your money – besides an overseas bank account or a stack of gold bars – is in **capital efficient stocks**. Particularly, ones in industries that perform well during a recession. You can think of capital efficiency as the ability of a company to convert its profits into shareholder returns, rather than having to sink them back into the business. Capital efficient stocks purposely return as much cash as possible to shareholders, which means that you're not just *protecting* your money – you're *growing* it.

A key thing to note: you're not playing the market here. Far from it. You buy only at the right price – which means you could be waiting years to get in. And you don't sell on a whim. You hang on to these equities for decades, so they build generational wealth. That's why I call them "forever stocks."

Forever stocks are virtually crash-proof. They're End-of-America-proof. And I honestly believe they're one of the safest places to store your money ahead of the coming crisis.

In this report, I'll introduce you to six of my all-time favorite "crash-proof equities" and explain why they're uniquely positioned to weather the storm. They include...

- The world's leading tobacco brand (because people keep smoking even during a recession)...
- A cash-rich coal exporter that will keep shipping black gold overseas no matter what...
- A "gold royalty" company that skims the profits off top gold miners without touching a shovel...

And three more... all featuring detailed write-ups from my research team at Porter & Co.

Please note that these are not official stock recommendations – but they are excellent companies that I highly encourage you to research and consider.

To your success,

Porter Stansberry

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Better Than Gold

Franco-Nevada (NYSE: FNV) - the “Gold Digger” That Gets Paid to Do Nothing – is the leading gold royalty company. Franco-Nevada provides financing for mining companies to do the capital-intensive work of pulling rocks out of the ground, in exchange for a percentage of the mine’s output. As a result, Franco-Nevada is highly capital efficient, generating 57% free cash flow (“FCF”) margins. Its world-class management team has established one of the best track records in the industry.

Franco-Nevada has a strong balance sheet with $1.4 billion in cash and no debt. On January 30, the company increased its dividend for the 17th consecutive year. The majority of Franco-Nevada’s earnings comes from royalties on gold mining assets. Gold typically performs well during recessions and market downturns, as investors flock to the safe-haven asset when the economy struggles. Plus, if history is any guide, global central banks will likely attempt to counter any economic weakness with interest rate cuts and monetary expansion – providing further upside to the already-record high gold price.

Better Than Gold

Franco-Nevada (NYSE: FNV) is a gold royalty company headquartered in Canada, in Toronto, Ontario.

Since going public in January 2008, FNV has grown into the leading global gold royalty company based on revenue and market capitalization.

It has long-standing partnerships to provide royalty and streaming financing deals to the largest mining companies on the planet. That includes the top three global gold miners – Newmont, Barrick Gold, and Agnico Eagle – as well as the leading diversified miners, including Glencore and Vale, along with dozens of smaller public and private miners.

The company's slogan is "the gold investment that works." Unlike most empty corporate slogans, FNV backs up this claim with performance.

FNV shares have outperformed the overall stock market, gold, and gold stocks since going public in January 2008:

This performance is a testament to the extreme capital efficiency of FNV's royalty business model. Because – here's the best part – FNV works without doing any work at all.

Franco-Nevada's World-Class Capital Efficiency

FNV is more like a bank than a mining company. It doesn't have to sink capital into expensive mining equipment, maintenance, and land claims… or hire geologists, engineers, and mining operators.

FNV runs its entire business with just 40 full-time employees and five part-time contractors. With just those 45 employees, the company generated $1.2 billion in revenue in 2023 and $695 million in net income.

That's more than $17 million in net income per employee – making it one of the most capital-efficient businesses in the world.

Capital efficiency describes how well a company transforms profitability into shareholder returns.

Virtually all companies have to reinvest some portion of their profits back into their businesses to maintain, replace, or upgrade fixed assets such as property and equipment (capital expenditures). Those that are able to spend less – that are efficient with their capital – are therefore able to pass along a greater proportion of their profits to shareholders.

Unlike mining companies that must funnel most of their earnings back into the business through capital expenditures, FNV's capital efficiency converts a high percentage of revenues into free cash flow (the amount of cash flow available after subtracting out capital expenditures).

In 2023, FNV generated $700 million in free cash flow for a 57% free cash flow margin. As a frame of reference, that's more than twice the 27% free cash flow margins of Microsoft – one of the best businesses in the world – and also better than the rest of the mega-cap tech cohort that has led the market in recent years (it also beats the 7% free cash flow margins of the world's two top gold miners, Barrick Gold and Newmont).

A "Gold Digger" That Doesn't Have to Dig

The long-term history of FNV's portfolio shows how deal-savvy the management team is when finding the right mines and operators to grow reserves over time.

When FNV first went public in 2008, the company had a $1.2 billion portfolio of assets with an average proven reserve base of more than 30 million ounces of gold.

Since then, that portfolio of assets has produced 45 million ounces of gold and generated $2.1 billion in royalties to FNV. And thanks to ongoing development and exploration at the mines which support those royalties, the reserve life of that same original portfolio has increased to roughly 70 million ounces as of year-end 2022, with no additional costs incurred by FNV.

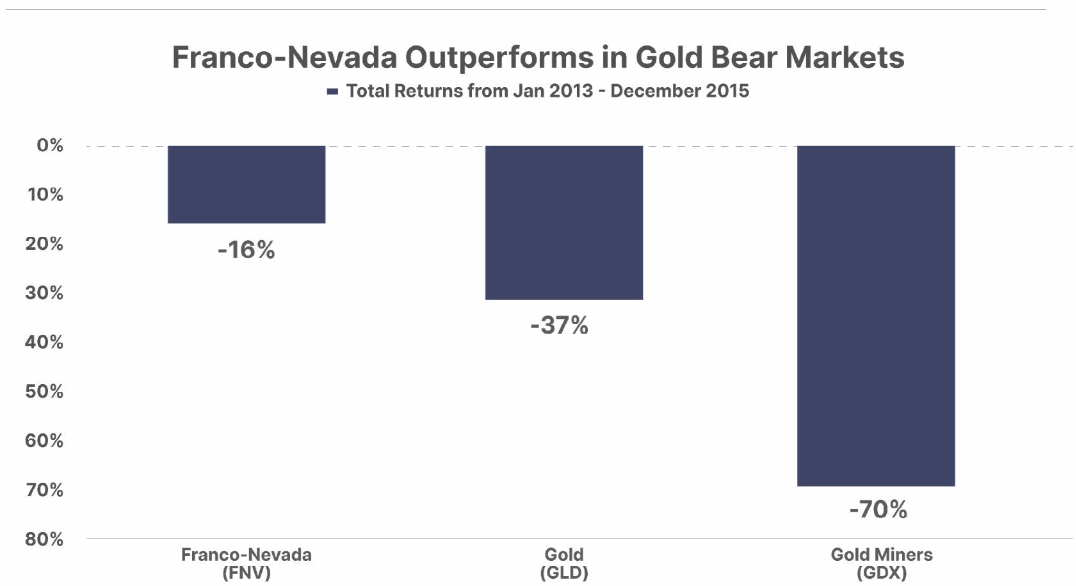
And that's where FNV's business model really shines. FNV strikes deals designed to recoup its original investment plus a double-digit rate of return while retaining future upside in perpetuity.

Most importantly, this future upside comes at no additional cost to FNV – its mining company partners foot the bill. When these miners sink money into the ground to grow their reserve base, FNV simply comes along for the ride.

Today, FNV owns a portfolio of more than 100 producing assets.

A True "Bunker" Stock

The other advantage of FNV's capital-efficient royalty model is that it protects against the downside. During the previous gold bear market from 2013 - 2015, FNV suffered losses of just 16% compared with a 37% decline in gold prices and a 70% drop in gold mining shares:



The company's outperformance in gold bear markets traces back to its capital efficiency. The most significant input cost for mining companies is labor. When gold prices fall, workers don't take kindly to pay cuts. Thus, gold miners get squeezed in bear markets when their operating costs remain elevated, and gold prices fall.

FNV, on the other hand, continues receiving its share of the gold produced, no matter how low gold prices go.

The same factors benefit FNV during bull markets, when input costs for fuel, equipment, and labor rise during periods of high inflation.

So while FNV takes a modest hit from lower gold prices, it doesn't suffer the same margin contraction miners incur during bear markets. And on the upside, FNV emerges from bull markets with substantially higher profits versus its mining peers.

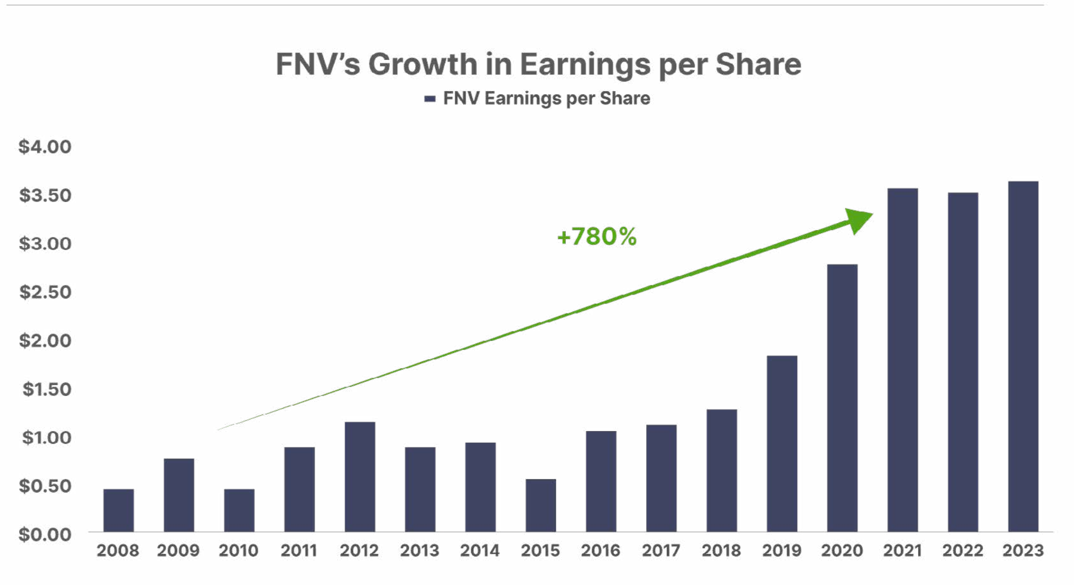
The final downside protection in FNV's capital-efficient business model comes from the company's ability to fund most of its growth through free cash flow, avoiding the risk of taking on excess debt.

For most of its history, FNV has maintained a pristine balance sheet with very little debt and lots of cash. Today the company has zero debt and $1.4 billion of cash on its balance sheet.

When FNV raises capital to accelerate growth, it typically issues shares.

Since going public in 2008, FNV has increased its share count by roughly 90%, from 100 million to 192 million shares outstanding as of year-end 2023. And the return on that capital raised has been spectacular.

Over the same period, the company's net income has increased 16-fold, resulting in earnings-per-share growth exceeding 750%:



Looking ahead, we expect this earnings trajectory to continue, based on our view of higher gold prices and FNV's ability to make great deals at the right mines with the right partners FNV offers the ultimate form of insurance against the growing risks of U.S. dollar devaluation.

The company's world-class capital efficiency and deal-savvy management team allow investors to both protect wealth and grow it over time, making it an ideal complement to your physical gold portfolio.

Not Your Grandpa's Tobacco Company

Philip Morris (NYSE: PM) owns the international rights to Marlboro, the world's leading traditional tobacco brand. Over the last decade, the company has invested heavily in less-harmful alternatives to traditional tobacco products. These investments have made Philip Morris the global leader in less-harmful nicotine consumption, including its hit IQOS and ZYN brands. Unlike most traditional tobacco companies suffering from declining sales, Philip Morris' smoke-free business is delivering double-digit revenue and earnings growth. The company is highly capital efficient, with 40% operating margins and a 27% average return on capital. Ittrades at an attractive 4.4% yield.

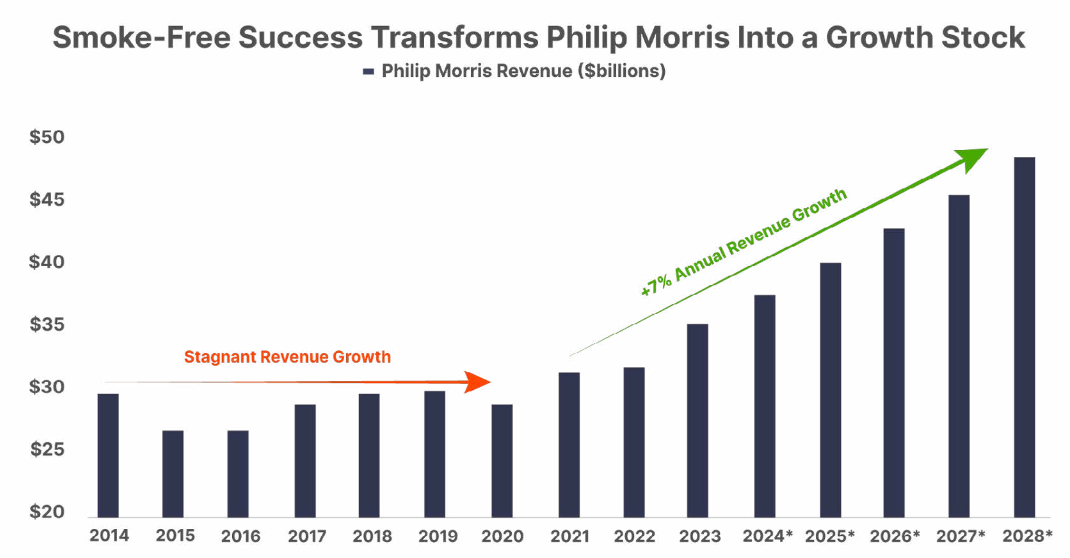
Best of all, the tobacco industry has historically been recession-proof. During economic downturns, when consumers cut spending on discretionary items, demand for tobacco products remains resilient or even increases. We expect this trend to remain in place going forward, both for Philip Morris's tobacco and smoke-free nicotine products. The combination of a recession proof business model, compelling valuation, and juicy dividend yield makes Philip Morris a compelling opportunity today, despite our expectation for an upcoming recession.

Not Your Grandpa's Tobacco Company

Philip Morris International (NYSE: PM) is the world's largest nicotine brand. Notice that we don't refer to it as a "tobacco company," as it was once commonly known. That was the original Philip Morris, founded in London in 1881, and which became the world's largest tobacco business selling the iconic Marlboro cigarette (among other brands).

The "new" Philip Morris is disrupting the status quo and leading the tobacco industry toward a new era of safer nicotine consumption. The company owns the world's most popular, less-harmful alternatives to cigarettes and chewing tobacco, known as "smoke-free" nicotine products. This includes its best-selling IQOS device, which heats (but does not burn) tobacco sticks – releasing a nicotine vapor that eliminates many harmful byproducts of burning tobacco.

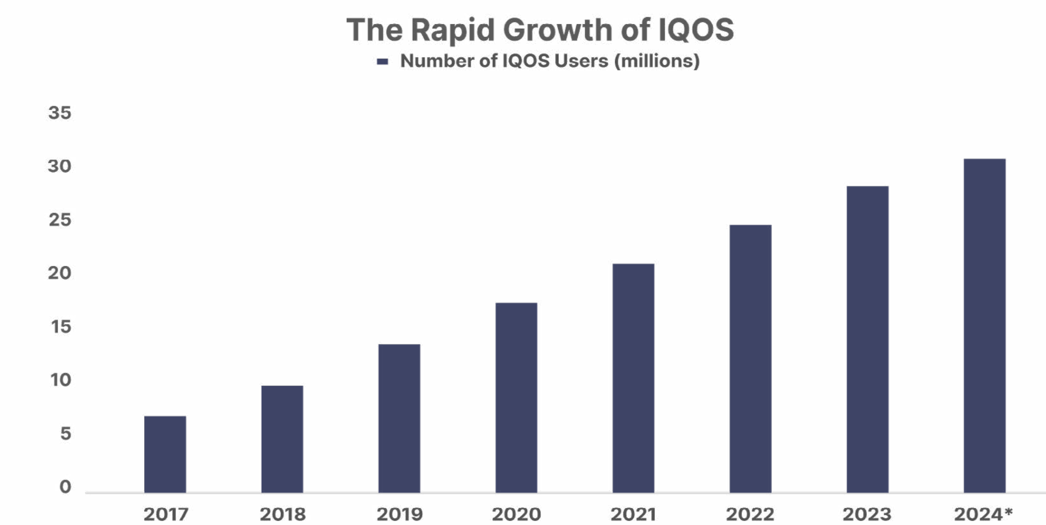
And unlike the traditional tobacco business of selling "cancer sticks," which is in long-term decline, Philip Morris' smoke-free business is booming. The sales from this segment have exploded from zero in 2014, to nearly 40% of the company's $35 billion in total revenue in 2023. This has transformed Philip Morris from a stagnant, old-economy tobacco company into a growth stock:



*Source: Bloomberg, *Analyst Estimates*

IQOS Was the Major Breakthrough Device

With its IQOS device, Philip Morris has been the most successful Big Tobacco company in separating nicotine from all of the harmful byproducts of cigarette smoke. IQOS was launched in Japan in 2014, and has since expanded into 90 countries. It's now the world's most popular and fastest-growing smoke-free nicotine device, reaching 30.8 million users in Q2 2024, up 2 million from the end of 2023. In the Japanese market, where the device first launched, IQOS now holds 30% market share among all tobacco products – including cigarettes.

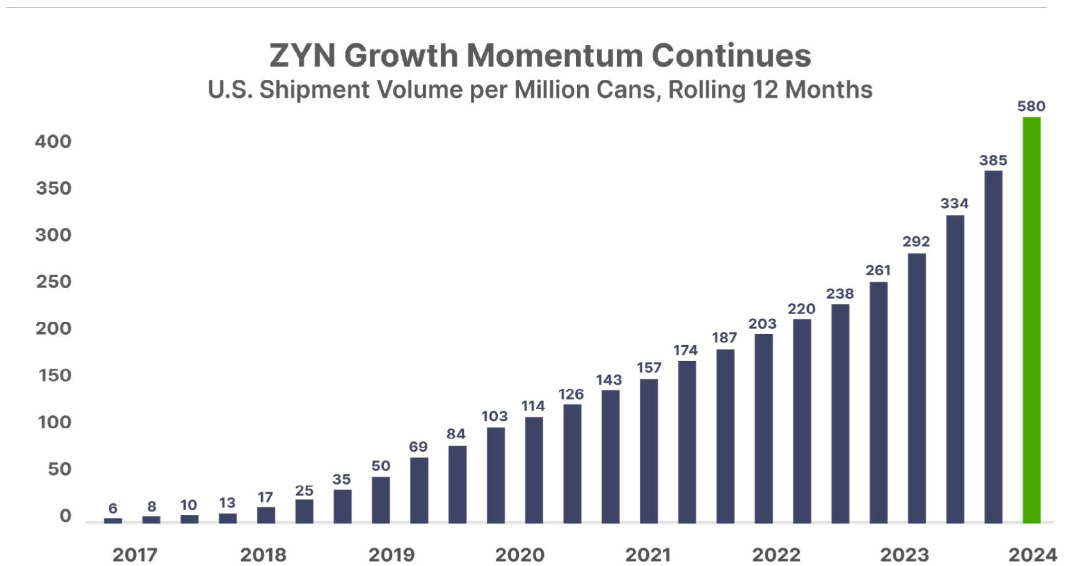


Source: Bloomberg; *Data through Q2

Philip Morris' other blockbuster smoke-free product is the ZYN brand of tobacco-free nicotine pouches. Nicotine pouches offer a less harmful alternative to chewing tobacco. Here again, the nicotine molecule isn't responsible for the mouth cancer caused from chewing tobacco. Instead, it's the 28 carcinogens that come from the tobacco plant and other additives used in the production process.

ZYN contains nicotine mixed together with food-grade ingredients, meaning ingredients that meet Food and Drug Administration ("FDA") guidelines and can be included in food. These ingredients are contained within a small pouch made of plant fibers, which releases the nicotine when moistened.

ZYN has become the global leader in nicotine pouches, including in its largest market of the U.S., where it holds 75% market share. ZYN sales in the U.S. are currently growing at 50% per year, reaching 135 million units in Q2 2024. The company is also generating strong international demand, where sales are up 60% in the first half of 2024. Demand continues exceeding all expectations, with the company revising up its forecasted sales twice so far this year. The company now expects to sell 580 million cans of ZYN in 2024, up 12% from the 520 million it anticipated at the start of the year.



Source: PMI financials or estimates, Circana, LLC, week ending 3/31/24

Not Giving Up Cigarettes Completely

Even as Philip Morris leads the world towards a smoke-free future, its legacy cigarette business will remain a cash cow for decades to come. That's because many of the international markets it sells into have maintained flat or growing cigarette volumes in recent years. And even when smoking rates begin declining in these markets, that won't stop Philip Morris from growing the revenues and profitability in its tobacco business. To understand why, consider the case of Altria - the former parent company of Philip Morris (before the two split apart in 2008) that owns the U.S. rights to the iconic Marlboro cigarette brand.

The U.S. tobacco market entered into long-term decline starting in the late 1990s, when smoking rates peaked and began dropping off by 2-3% per year. From the late 1990s through 2020, Altria offset falling U.S. cigarette volumes with higher prices, allowing the company to post consistent revenue and profit growth over those two decades. Only in the last few years, when volumes began declining at double-digit rates, has Altria suffered from revenue declines (and still small at less than 2% per year on average). This gives us confidence in Philip Morris maintaining a long tail of profitability and revenue growth from traditional tobacco sales, even as smoke-free products make up a larger part of its business.

And unlike many companies that must make a trade-off between investing in future growth and milking cash flows, the company is enjoying the best of both worlds. That's because the nicotine business, both traditional tobacco and RRPs, are capital efficient. These products, once developed, require minimal capital expenditures relative to the revenue and cash flows they generate. This shows up in Philip Morris' impressive free cash flow margins, which have averaged 30% a year over the last five years.

Shareholders reap the benefit of its high capital efficiency, as the company returns a big chunk of its $10 billion in annual free cash flow as dividends. The company currently pays out $8 billion per year in dividends, through a $1.35 quarterly payout, or $5.4 per year. This represents a yield of more than 4% at PM's current share price. 4.4% annual yield at PM's current $118 share price.

With the world's best smoke-free nicotine products, and a resilient legacy tobacco business, Philip Morris grew revenue by 11% in 2023. And it's on pace for an average of 7% annual revenue growth over the next four years, based on analyst estimates.

Meanwhile, management expects the company to generate $6.39 in earnings per share in 2024, or 12% growth versus 2023. Best of all, given the addictive nature of its product, we can expect Philip Morris' revenue and earnings trajectory to remain intact despite the threat of a recession or any other economic shock, in the same way that traditional tobacco products have historically shrugged off economic downturns.

In our experience, one thing savvy investors won't ignore for long is when a company consistently beats high expectations, and continues raising the bar – especially when it's trading at a discounted valuation. More recently, close market watchers have started paying more attention, as evidenced by the significant increase in Philip Morris' share price so far this year – including a 26% gain year to date, or 11% better than that of the overall market.

We believe the tide has shifted and investors are now waking up to the opportunity in PM shares. As the company continues delivering on product sales, revenue, and earnings across the board, it's becoming too "inevitable" to ignore. And yet, the shares remain attractively priced, for now.

At $118 per share, PM currently trades for less than 18× 2024 projected earnings – a 15% discount to the S&P 500's 21x forward earnings multiple. Given the company's double-digit earnings growth rate, consistently high free cash flow margins, and its recession-proof business model, we believe PM shares should command a significant valuation premium, rather than a discount, over the broader market.

This has all the ingredients of a high-conviction opportunity, when investors can make money with almost 100% certainty. We think PM shares could reach a 25x valuation multiple, or $160 per share. From there, we see double-digit annual compounding potential, in line with Philip Morris' future earnings growth outlook. Best of all, investors get paid to wait for the share price to rise, as the company pays out a healthy 4.4% dividend yield.

Coal to the World

Consol Energy (NYSE: CEIX) is one of America's leading producers of thermal coal, which is the type of coal used for electricity generation. The company is one of America's best-positioned coal miners to thrive despite the regulatory headwinds facing the industry, thanks to its ultra energy-dense coal that generates electricity with fewer carbon dioxide emissions than the competition. Consol also owns a key exporting terminal that gives it a low-cost advantage for exports into international markets. With global coal demand setting new record highs, Consol's booming export business makes it one of the few U.S. miners with production volumes reaching new record highs, including 9% growth in output in 2023.

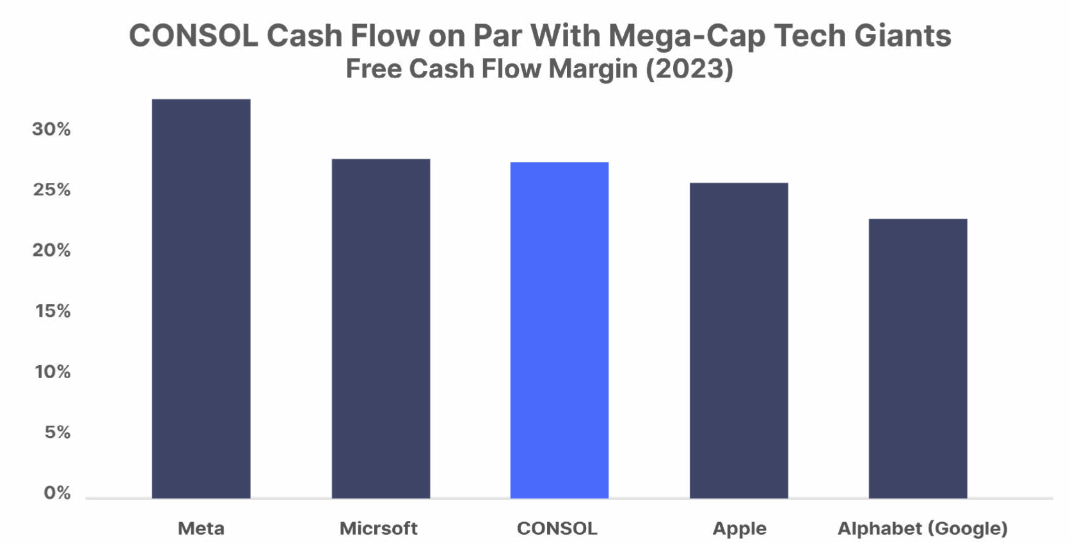
Trading at just 7x earnings, Consol shares offer a rare margin of safety in today's richly priced stock market, with the S&P 500 trading at 21x earnings. The company also has a pristine balance sheet that contains more cash than debt, providing resilience against an economic downturn. Meanwhile, the company generates tremendous free cash flow margins that exceed 25%. The company returns a lot of that cash to investors through buybacks, which have reduced its share count by 18% in the last two years alone. With a robust balance sheet and ample free cash flows, the company is well-positioned to capitalize on any volatility in its share price by repurchasing shares at an attractive valuation.

Coal to the World

Headquartered in Cecil County, Pennsylvania – just outside of Pittsburgh – **CONSOL Energy (NYSE: CEIX)** is one of America's oldest coal producers. Its parent company Consol first began mining in 1864 in the Appalachian Basin, one of America's richest coal deposits. CONSOL Energy was spun off and began trading as a public entity in 2017.

CONSOL Energy primarily produces thermal coal, which is used to generate electricity. In 2023, the company mined 23 million tons of thermal coal, making up 88% of its total output. The remaining 12% of production was metallurgical coal, which is used in steel-making.

In total, the company mined 26.1 million tons of coal in 2023, up 9% from 2022. This brought in $2.57 billion in revenue and $687 million in free cash flow, for a stellar free cash flow margin of 27%. For perspective, that's on par with some of the world's most dominant technology giants, including Microsoft, Meta, Apple, and Alphabet (Google):



Source: Bloomberg

Despite CONSOL's impressive profit margins, it gets little respect on Wall Street. Many hedge funds, pension funds, and market index providers simply won't own coal stocks for fear of being labeled "non-woke."

At Porter & Co. we're more than happy to capitalize on the folly of the woke ideologues. Wall Street's dislike of coal stocks has created a tremendous opportunity in shares of CEIX, which trade at a deeply discounted valuation of just 5x free cash flow. In contrast, today's much-loved mega-cap technology stocks command valuations of 30x to 60x free cash flow multiples. This dirt-cheap valuation makes CONSOL one of the most unloved, underappreciated winners of the parallel-computing revolution.

One of the key factors behind CONSOL's resilience is the superior quality of its mining assets... and the other is the low cost of its mining operations.

The Secrets to CONSOL's Success

CONSOL's core cash cow, responsible for 99% of its coal production, is a collection of mining properties in northern Appalachia that make up the Pennsylvania Mining Complex ("PAMC"). Together, these three mines generated a total of 26.1 million tons of coal in 2023.

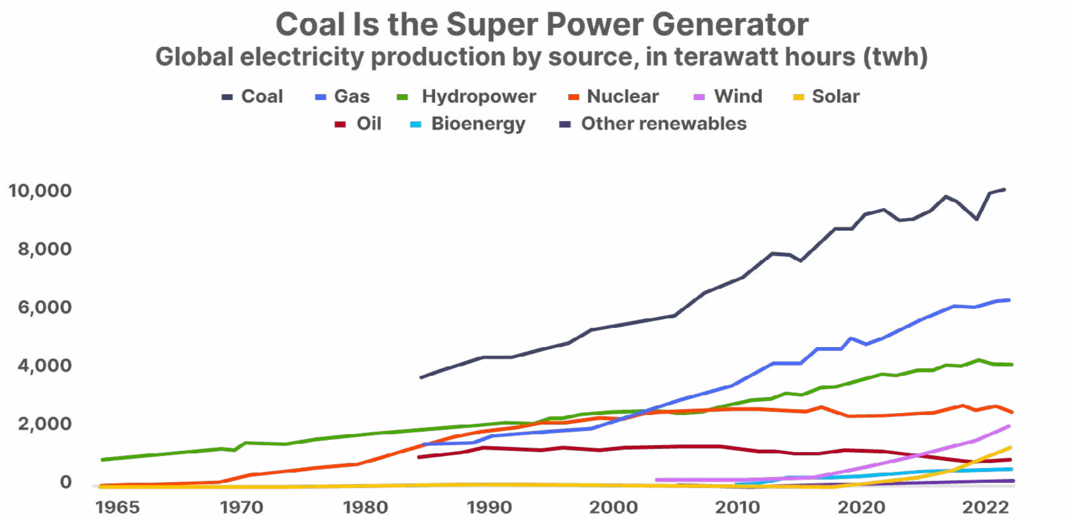
Appalachia is home to some of the most energy-rich thermal coal in the U.S., and the energy density increases toward the northern end of the basin. CONSOL's PAMC mines contain some of the most energy-rich coal among all major U.S. coal basins, with an average of 12,972 British thermal units (Btu) per pound. This is up to 50% more energy-rich than other major U.S. thermal coal basins Six of CONSOL's top domestic power plant consumers, which each purchase over 500,000 tons of coal each year (2% of CONSOL's output), have been customers for at least five consecutive years. Securing long-term relationships with stable utility operators is one key reason why CONSOL has managed to grow its coal volumes more than 5% from 24.8 million tons in 2017 to 2023, even as the overall industry has suffered double-digit volume declines over that same period.

The other advantage of CONSOL's PAMC mines is that pulling coal from this area is a low-cost operation. That's because of the Pittsburgh Number 8 Coal Seam, the geological formation that hosts PAMC's energy-rich coal. Coal seams are long, continuous rock formations that enable what's known as "longwall" mining. This process involves shearing off large, slices of coal-containing rock from a long face (or wall) of a geological formation in a single pass.

Longwall mining is safer, faster, and more economically efficient than underground mining methods, like the "room and pillar" method, which requires digging into an underground coal formation, creating a mining "room" for extracting coal, while leaving large "pillars" of the formation in place to support the roof.

By eliminating the need to dig elaborate underground structures, it requires less man and machine power per unit of coal mined. Underground mining methods like room and pillar typically only recover about 50% to 60% of the available coal deposit, compared with more than 75% that longwall mining extracts.

And CONSOL's future as a coal miner isn't limited to a declining U.S. market. Coal offers the cheapest, most reliable form of baseload energy in the world. So even as climate alarmists have hurt demand in the U.S., the rest of the world continues building new coal-fired power plants. That's why coal consumption recently hit all-time highs in 2022, following a brief decline in 2020-2021 when global economic activity slowed during the COVID-19 pandemic:



Source: Ember, Energy Institute

Most experts forecast that global coal demand for power generation will continue growing through at least 2030. The key drivers of this demand will come from India and China, which together make up one-third of the world's population. In 2023 alone, China grew its coal capacity by 48.4 GWs (or 4%), while India added 14 GWs of capacity.

The massive (and growing) global market for thermal coal means that, even in the ultimate bear case scenario where U.S. coal consumption goes to zero, CONSOL can still thrive.

That's all thanks to CONSOL's ownership of a key export terminal, strategically located to deliver a low-cost advantage for coal shipments into international markets.

How CONSOL Gets Coal to the World

Perhaps CONSOL's most valuable asset is its Marine Terminal, located in the Port of Baltimore. This is the only major east coast coal terminal that can receive shipments from two railroad operators, Norfolk Southern and CSX. The terminal includes 19.3 miles of railway track, with three railway sidings, which are short tracks used for loading and unloading freight that do not interfere with the main line operations. This infrastructure allows the CONSOL Marine Terminal to seamlessly load coal directly from rail cars to shipping vessels, with a capacity of up to 9,000 tons of coal per hour (or 78 million tons per year, or around three times CONSOL's total annual production).

Ownership of this port infrastructure provides several key competitive advantages for CONSOL. The first advantage is the port's location, only 250 miles from the PAMC mining complex in Northern Appalachia. This short hauling distance provides

CONSOL with one of the lowest transportation costs for moving its coal from the mine site to export ships, at an average cost of just $18 to $19 per ton, which is 15% to 20% cheaper than the $21 to $25 cost of moving coal from other key U.S. basins to alternative export terminals. In addition, CONSOL doesn't have to pay a third party to handle its coal at the terminal, which provides further cost savings.

Since 2017, CONSOL has doubled its export coal sales from 8.3 million tons (or 32% of its total volume) to 16.2 million tons in 2023 (or 61% of total volumes).

A Diamond in the Rough

With stock prices trading at record-high valuations across the board, CONSOL is an exception, offering a rare, deep value opportunity.

With its rich asset base of low-cost mines in the heart of America's richest coal basin, plus its strategically located Port of Baltimore marine terminal, CONSOL has produced positive free cash flows every year since going public in 2017 – including in 2020, when coal prices collapsed during the COVID-19 outbreak.

The company's steady cash flows support a pristine balance sheet with more cash than debt, allowing it to funnel its excess cash to investors. CONSOL's shareholder-friendly management team has committed to returning 75% of cash flow to investors, primarily in the form of share repurchases. In the last two years alone, the company has reduced its share count by nearly 20%.

The combination of growing production volumes and cash flows, plus a falling share count, has propelled CONSOL's earnings per share nearly 10-fold since going public, from $2 in 2017 to $19.64 in 2023.

Even though the company gets little attention on Wall Street, and thus trades at a deeply discounted valuation, its share price has handily outperformed the market. Since 2017, CONSOL has delivered a 364% total return, or 27.6% compounded annual growth rate ("CAGR"). Over the same period, the S&P 500 has gained 106%, or a 13.6% CAGR.

Given its deeply depressed valuation of just under 5× 2023 free cash flow, CONSOL is one of our top stocks to watch that will capitalize on today's parallel computing boom. Plus, a recent deal has further brightened the long-term prospects for CONSOL.

On August 21, CONSOL announced it reached a merger agreement with fellow coal miner Arch Resources (NYSE: ARCH) to form a new entity called Core Natural Resources.

The deal terms state that CONSOL shareholders will own 55% of the merged entity, with Arch shareholders owning the remaining 45%. Arch investors will receive 1.326 shares of CONSOL in exchange for each share of Arch owned as of

August 30. When the deal closes, CONSOL shares will be converted to the new entity Core Natural Resources.

The companies expect the merger will close by the end of Q1 2025, pending approval by shareholders of both companies and U.S. regulators.

We like this deal for two reasons.

1. Arch is one of the leading low-cost producers of metallurgical coal – the type used in steelmaking. Unlike thermal coal, which is being phased in the U.S. and Europe due to environmental restrictions in favor of cleaner-burning fuel sources, metallurgical coal has no viable substitute in the steelmaking industry. As a result, the long-term demand for metallurgical coal will continue rising with global economic growth indefinitely. The newly combined entity will thus have a highly diversified portfolio that will ensure decades of future demand ahead.

2. It will eliminate operational redundancies between the two companies, unlocking an estimated $110 million to $140 million of cost savings within six to 18 months of closing the transaction. As a result, the deal is expected to generate positive free cash flow for both Arch and CONSOL in year one of the merger.

Following the news of the merger on August 21, CONSOL shares rose 5% to $100 per share (or a $3.0 billion market capitalization) while Arch rallied 3% to $130 per share (or a $2.4 billion market capitalization). At these prices, this implies a combined market value for the merged entity of $5.4 billion. Additionally, both companies have a positive net cash position totaling $260 million, which puts their combined enterprise value (market capitalization plus net debt) at just under $5.2 billion.

This is a compelling valuation considering both companies generated a combined total of $1.8 billion in EBITDA (earnings before interest, taxes, depreciation, and amortization) and $1.4 billion in free cash flow last year. Adding in the expected cost savings of $125 million (at the midpoint of CONSOL management's guidance), this puts the implied valuation of Core Natural Resources at approximately 2.7x EV/EBITDA and 3.5x EV-to-free cash flow.

We view this is a compelling valuation of the newly combined entity based on the current share prices for both CONSOL and Arch. Longer term, we're optimistic about the prospects of Core Natural Resources as a leading, low-cost producer of both thermal and metallurgical coal.

As a result, we are recommending investors hold shares of CONSOL in order to eventually own shares of Core Natural Resources following the closing of the merger in Q1 2025.

For CONSOL investors, no action is needed. The CONSOL shares will be converted automatically to stock in the newly formed Core Natural Resource after the deal closes.

The Safe Way to Play the AI Boom

Deere & Company (NYSE: DE) is the world's leading provider of farming equipment and crop management tools, with a trusted brand that's become synonymous with quality and reliability over its nearly 200-year history. In addition to its brand power, Deere benefits from a significant scale advantage that allows it to spend nearly 50% more than its largest competitors combined on research and development each year. More recently, Deere has aimed its R&D budget into developing the world's most advanced automation and precision-farming tools and software. This is transforming Deere from a pure hardware manufacturer towards a technology company, with stickier customer relationships and higher-margin, recurring revenue.

Deere will perform well even during a potential recession because the key driver of its business – the agricultural cycle – tends to operate independently of the economic cycle. In fact, the farming industry is already deep into a recession, with high interest rates and depressed crop prices putting Deere's earnings on pace for a 32% drop this year. We remain optimistic on Deere's future earnings potential, though, given that interest rates and the U.S. dollar have likely peaked. With the Federal Reserve on track to begin cutting rates in response to economic weakness, this will lower borrowing costs for farmers, making Deere's equipment less expensive to finance. Plus, rate cuts will likely lead to a weaker U.S. dollar, which has historically translated into higher crop prices. With the shares trading at just 14x earnings, and the worst of the agricultural recession likely behind us, Deere offers a compelling value today.

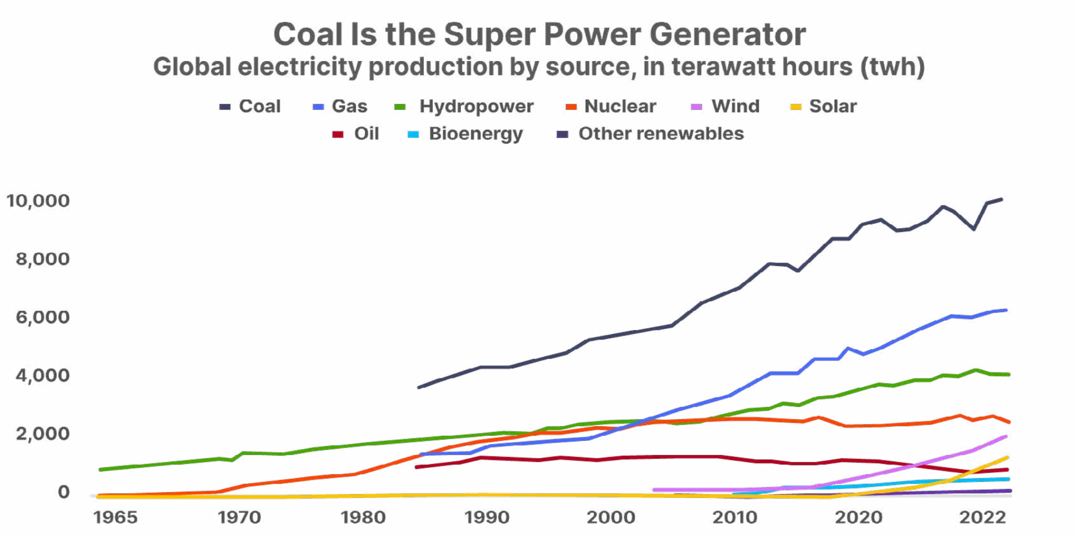
The Safe Way to Play The AI Boom

Deere is the largest seller of agricultural equipment in the world, with 18% global market share. In its key U.S. geography, Deere controls roughly 60% of the market in tractors and combines. And its leading brand power developed over the last two centuries has translated into unmatched customer loyalty. Deere consistently ranks at the top of the brand-loyalty rankings from Progressive Farmer, one of America's longest-running agricultural magazines. Survey results from the publication indicate 52% of Deere customers are brand loyal, compared with 42% for its next closest competitor.

Historically, Deere's esteemed name and customer loyalty provided its greatest leg up. But today, the company's sheer size compounds that competitive advantage.

Deere currently generates $61 billion in annual sales. That's more than double the $25 billion in sales from its next closest competitor, CNH Industrial (CNHI), and more than four times its next closest rival AGCO (AGCO), with $14 billion in sales.

This larger revenue allows Deere to invest more in research and development (R&D). Deere currently plows about $2 billion into R&D, or roughly 50% more than the combined R&D budget of CNH and AGCO.



Source: Ember, Energy Institute

In the past, Deere's product development centered around larger engines and bigger equipment. In the age of mechanized farming, covering more ground faster was the name of the game. But since the turn of this century, digitization and automation have become the new frontier in boosting productivity.

These early technologies have set the foundation for Deere's more recent push into AI and fully autonomous farming equipment. And along the way, they've transformed Deere's business from a pure hardware manufacturer into a higher-margin technology company, while cementing its competitive edge against rivals.

Let's take a look at how these early forms of advanced technology have set the stage for Deere's future trajectory.

How Deere Is Becoming a "Stealth" Software Company

In 2002, Deere introduced Autotrac, one of the world's first self-steering features for commercial crop equipment. Deere developed its own StarFire GPS (global positioning system) network with NASA engineers at the space agency's Jet Propulsion Laboratory in California. The current version can position Deere's equipment to within 5 centimeters of precision.

Then in 2012, Deere introduced the IOT age (internet of tractors), when it began installing telematic devices across its full line of large machinery. These devices allow machines to synchronize with one another using Deere's Machine Sync technology. As one example, during harvest time, this software coordinates the movement of harvesters with loading trucks. During the critical harvest season when every second counts, this coordinated movement saves farmers significant time and money.

Deere has also invested heavily into data-management systems, including the John Deere Operations Center, opened in 2013. This Center compiles data from Deere's machines in the field, which analysts use to help farmers optimize operations. First it was efficient plows. Then faster tractors. Now, data gathering and analysis have become key drivers of boosting productivity on modern farms.

When farmers employ Deere's connected equipment and information management system, it creates a natural incentive to choose Deere for their next equipment purchase. That's because each added Deere machine can work in concert with the rest of a farmer's connected fleet, and it contributes field data into its sophisticated Operations Center for analysis and optimization.

Over time, this creates a stickiness to the Deere brand because of the tremendous cost of switching to alternative equipment providers. If farmers move away from Deere's ecosystem, they lose access to the precious data they've collected to optimize operations.

The automatic-guidance and data-management systems Deere invested into over the last two decades provided the foundation for its next big technological push – into AI, starting in 2017.

Deere jump-started its AI trajectory with two key acquisitions, including the $305-million purchase of Blue River Technology that year and the $250-million purchase of Bear Flag Robotics in 2021. Both of these Silicon Valley-based companies had developed cutting-edge, AI-based software designed to enable autonomous farming equipment. The technology Deere acquired enabled the company to make the leap from limited self-guidance systems to today's new era of fully autonomous agriculture.

One hundred years after ushering in the era of mechanized farming with the iconic Model D, in January 2022 Deere unveiled the Model 8R – the world's first fully autonomous, self-driving tractor.

In the coming years, Deere plans to roll out automation across its full portfolio of large machinery including combines, planters, and fertilizer sprayers. This is all in pursuit of its bold 2030 objective: to create the world's first fully autonomous farming system.

Deere envisions creating a full suite of fully autonomous machinery for every stage of crop production, from planting to harvest. The first iteration of the 8R requires a human in the tractor to oversee its operation. But the company is aiming for a future where its equipment can operate completely free of human operators.

A Big Opportunity With Deere's Big Data

The high-resolution cameras in Deere's equipment provide an increasingly valuable trove of data that can be analyzed to optimize every aspect of crop production. Deere feeds this data through its Deere Operations Center, which uses machine learning to provide valuable insights into everything ranging from yields, performance of herbicides and fertilizers, and moisture levels.

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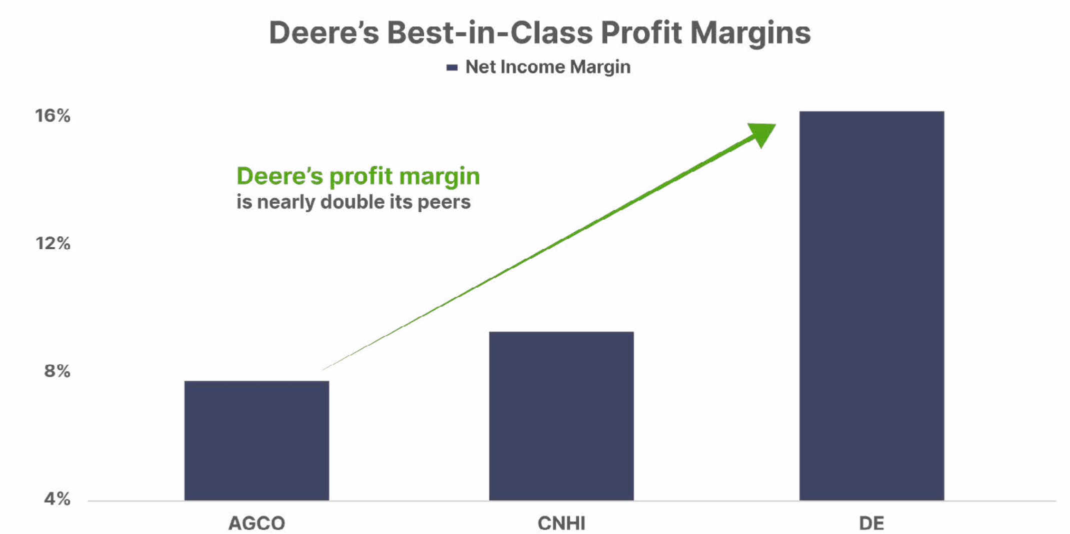
The company currently has over 500,000 connected machines feeding data to its Operations Center. This provides an unmatched set of data containing billions of measurements on soil, crop, and weather conditions. Deere's machine-learning software can draw critical insights from this data to help farmers optimize every part of their operation.

And this unmatched fleet of connected machines will create an ever-expanding competitive advantage over Deere's rivals. As more Deere machines connect to Deere's network, the more powerful its insights will become from the growing source of data feeding into its network. This will greatly improve the company's profitability and further cement Deere's advantage over its rivals, who simply can't compete with the company's unmatched installed base of data-gathering equipment.

Deere's widening competitive moat translates into unmatched pricing power. Deere's products command a premium over its competitors, and the company routinely raises prices even when the industry enters a downcycle – including during 2014-2016. During the good years, Deere raises prices well above rates of inflation, including a 12% average increase across its product portfolio in 2023. Deere's pricing power translates into industry-leading 16% profit margins, or nearly double those of its top rivals.



Source: Bloomberg

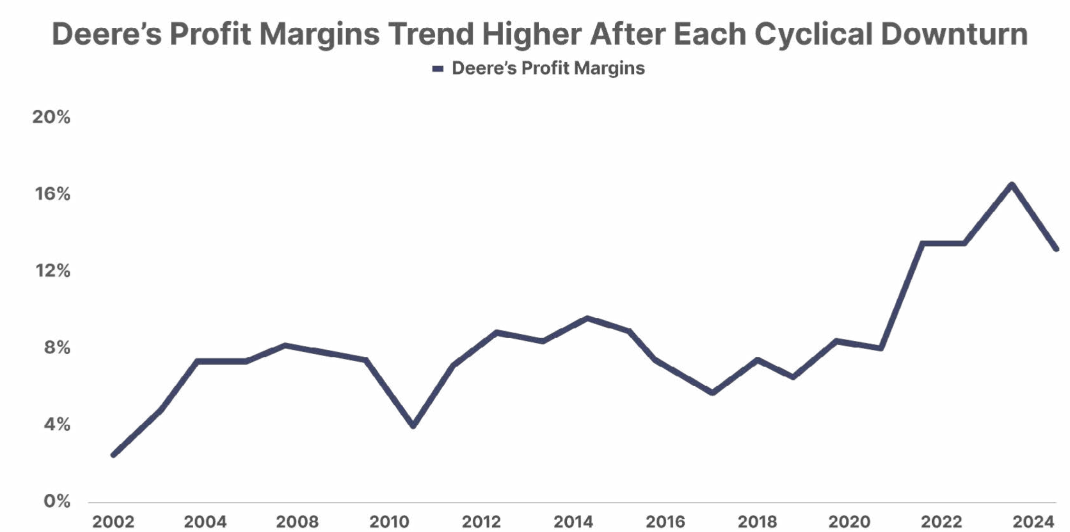
The Safe Way to Play the AI Boom

Thanks to its number-one position in the industry, Deere enjoys a tremendous scale advantage. It can invest more in R&D and acquisitions than its competitors. As the business of farming evolves into the new era of autonomous and precision agriculture, optimized by big data and machine learning, Deere will only strengthen its position.

Even through the ups and downs of the crop cycle, Deere's revenues have steadily increased over the long run, up 300% in the last two decades. Over the same period, Deere's net income has risen 7x, or more than double the rate of revenue growth.

We believe this long-term trend toward margin expansion will continue as the company introduces the next generation of AI-based farming equipment and software. Deere's net income margins reached new all-time highs of 16% in 2023. However, even as the company becomes more profitable over the long run, the business still takes a short-term hit during the inevitable downturns in the agricultural cycle. Falling crop prices have pressured Deere's sales in 2024, causing the company's margins to fall by three percentage points down to 13% this year.

We can't predict when the current crop cycle will reverse. But one thing we do have confidence in is that Deere's long-term trend of higher profitability will continue when crop prices rebound. The chart below shows that Deere's margins inevitably recover from each down cycle to reach new record highs:



Source: Bloomberg

Deere's business is very capital efficient, generating 25% operating margins and 35% returns on equity. This high capital efficiency allows the company to return substantial profits to shareholders. Over the last 20 years, the company increased its dividend 10-fold from $0.14 per share to $1.47 today. Over the same period, consistent buybacks have reduced the share count by 45% from 500 million to 275 million.

The combination of growing revenues, expanding profit margins, and a shrinking share count has fueled a rapid rise in earnings per share (EPS). Over the last two decades, Deere's EPS has increased more than 10-fold, from $2.78 to $34. That's how the company has delivered world-class 16% annualized returns for investors over the last two decades – compared with 11% annualized returns in the overall market (S&P 500).

While many of today's tech stocks associated with AI trade at sky-high valuations (like NVDA's 50x price-to-earnings ratio), Deere trades at a bargain price of less than 13x expected 2024 earnings– near the low end of its historic range of 10x to 30x.

Normally, the market would command a premium for this kind of business. But at less than 13 times earnings today, Deere offers substantial upside from its new AI technologies, with a wide margin of safety.

The Bankruptcy King

Houlihan Lokey (NYSE: HLI) is the leading provider of advisory services for corporate bankruptcies. The company has advised on over 1,500 corporate reorganizations, with total debt claims exceeding $3 trillion since 1988. This includes some of America's most high-profile bankruptcies like Lehman Brothers, General Motors, Enron, and WorldCom. This will make Houlihan Lokey one of the biggest winners from the record-setting corporate default cycle that we see coming. In fact, it's already beginning, with U.S. corporate defaults recently reaching the highest levels since 2017.

But Houlihan doesn't need a credit bust to thrive. The company is also an industry leader in two other business segments: corporate finance (raising capital) and valuation advisory services. Both of these business units can do well during good economic times. During bull markets, corporate demand for raising new equity or debt capital is typically robust. Likewise, demand for corporate transactions like mergers and acquisitions provides a boost to Houilhan's valuation advisory services during bull markets.

The Bankruptcy King

The world economy is on the precipice of a debt crisis unlike any that's ever happened before.

Because of soaring inflation, the world's central banks can no longer deliver the stability that markets have gotten used to. The global economy is facing a complete reset of interest rates, sovereign debt loads, and corporate debt loads without the "cushion" of central bank largesse to soften the collapse.

We call this once-in-a-lifetime credit supercycle **"The Greatest Legal Transfer of Wealth in History,"** because an incredible amount of money will be changing hands as the market melts down.

In the coming months there will be an unprecedented number of companies in distress… which leads us not only to discounted bond buys, but also to truly shaky companies that need help restructuring in order to keep afloat. And that's where HLI comes in.

A Capital Efficient Business That Thrives in All Market Conditions

Companies that focus on financial restructuring are a countercyclical hedge across macroeconomic cycles. When the economy dips, HLI and similar companies benefit… just like when a global pandemic strikes, it's the vaccine makers that thrive.

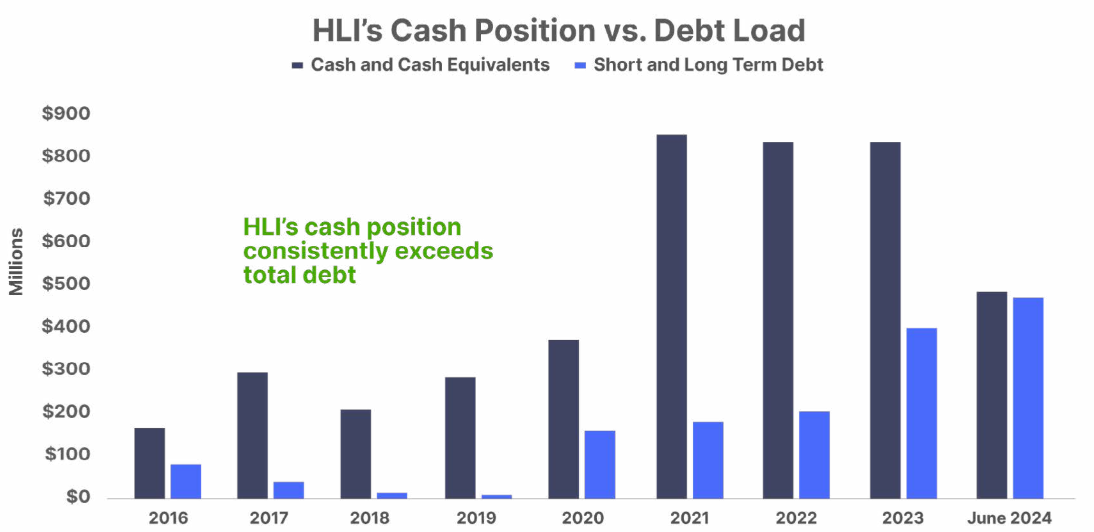
HLI is run by industry experts who have deep experience evaluating leveraged restructurings. For non-finance types, it's off the radar – based in Los Angeles… some 2,800 miles west of Wall Street.

Houlihan Lokey Howard & Zukin was founded in 1972 by Richard Houlihan and O. Kit Lokey, who'd worked together at consulting and accounting giant PriceWaterhouse (now called PricewaterhouseCoopers or PwC Today, the company advises large corporations worldwide on deals, fairness, and restructuring, in offices around the world.

HLI has advised on over $10 trillion in deals over its five-decade history. It is diversified across a wide set of geographies, industries, and business segments with a focus on mid-cap firms (between $2 billion and $10 billion in market cap).

By maintaining a broad, diverse base of clients, HLI can apply its extensive experience to plumb the market dynamics affecting each restructuring situation. HLI advises both companies and creditors – it serves more than 2,000 clients each year – at all levels of the capital structure, to provide holistic advice to their clients. No client base segment accounts for more than 18% of revenues. It's built its business in part through buying the best of its peers and competitors.

HLI maintains a rock-solid balance sheet, with cash and cash equivalents consistently greater than its outstanding debt.



Source: Bloomberg

It's a highly capital efficient business model. HLI generates more than $700,000 in revenue per employee while its free cash flow margins have averaged 22% over the past five years. This means HLI can return capital to shareholders, via generous share repurchases and dividends. Over the last decade, HLI has returned $1.6 billion to investors through share buybacks and dividends, or about 15% of its current market value. The company currently pays out a 1.5% dividend.

How Houlihan Lokey Works

Houlihan Lokey has three major divisions, and it's a market leader in all of them: Corporate Finance, Financial Restructuring, and Financial and Valuation Advisory. HLI was the #1 M&A advisor globally based on the number of transactions in 2023. It's also the #1 most active fairness opinion advisor by volume for the past 25 years.

And – most interesting to us – it's the #1 *restructuring advisor* globally, based on deals and value. It has the largest restructuring practice of any investment bank worldwide, completing 1,500 reorganizations with total aggregate debt claims over $3 trillion since 1988.

The firm's Corporate Finance group serves companies, funds, and governments. Its main service is M&A: helping companies buy and sell themselves and their divisions. In its latest fiscal year 2024 (ending March 2024), Houlihan earned $1.1 billion in corporate finance fees. Houlihan Lokey helped close 450 transactions in the year ended March 2024.

Its second division, Financial and Valuation Advisory, serves as a kind of third-party "Kelley Blue Book" for companies, to evaluate businesses' debt, shares, and deals.

And the third division, Financial Restructuring, is the one that will be key during the current credit cycle.

Right now, we're entering an unprecedented credit meltdown that we like to call **"the greatest transfer of wealth in history."** Now, with the end of the easy money era, many companies will run out of liquidity and face bankruptcy. And that's where skilled restructuring firms like HLI come in.

In the wake of the global economic crisis, the Federal Reserve created nearly $8 trillion in new credit, while keeping interest rates pinned at zero. That allowed fundamentally unsound companies to borrow like there was no tomorrow.

But now, higher interest rates are creating deep distress for an economy built upon the fragile foundation of cheap money. In the second quarter of 2024, the number of U.S. corporate bankruptcy filings reached 6,276. That's more than double from the recent lows of 3,065 in Q1 2022, and the highest level since Q2 2017.

The coming corporate default wave will also create another "ripple effect" opportunity. We're about to see a corresponding boom in the restructuring business: last-ditch interventions for companies on the verge of bankruptcy. And that's where Houlihan Lokey excels.

More Bankruptcies Means More Restructuring

Big, headline-grabbing bankruptcies like General Motors, Lehman Brothers, and Enron generally have two things in common: They're Chapter 11 filings, meaning the company is allowed to restructure and reorganize. And: Houlihan Lokey has been involved.

Houlihan Lokey advised major parties-in-interest in 12 of the 15 largest corporate bankruptcies in the U.S.

Advisor in 12 of the 15 Largest Bankruptcies 2000-2022

Company	*Assets ($bn)*
Lehman Brothers Holdings Inc.	691.1
Washington Mutual Inc.[1]	327.9
WorldCom Inc.	103.9
General Motors Corporation	91.0
CIT Group Inc.	80.4
PG&E Corporation (Pacific Gas) (2019)	71.4
Enron Corp.	65.5
Conseco Inc.	61.4
Energy Future Holdings Corp.	41.0
MF Global Holdings Ltd.	40.5
Chrysler LLC	39.3
AIG Financial Products Corp.	37.7
Thornburg Mortgage Inc.	36.5
Pacific Gas & Electric (2004)[2]	36.2
Refco Inc.	33.3

(1) Houlihan Lokey advised certain creditors of the Washington Mutual Receivership. (2) Houlihan Lokey advised a group of noteholders of Pacific Gas & Electric subsidiary National Energy Group Inc.
Source: BankruptcyData.com and Debtwire, January 2023.

Chapter 11 reorganizations have several goals: consolidating debts so that creditors receive as much cash back as possible; giving the distressed business "breathing room" to get back on its feet; and, most importantly, offering a fresh start with a new balance sheet for a company that would otherwise be liquidated.

Along the way, the structure of the business may change drastically, with layoffs, reorganizations, or new management. And Houlihan Lokey is there for the pain. With 35 offices worldwide, HLI has a finger in every flavor of bankruptcy pie imaginable. In 2022, as Chapter 11s ticked up sharply, Houlihan Lokey advised on more global distressed debt deals than any other investment bank.

The latest Chapter 11 boom is just getting underway as recession rumblings begin, and Houlihan Lokey has already seen its restructuring revenue rise over the past two years. In the company's fiscal year 2024, the Financial Restructuring segment closed 126 transactions, up 40% from 90 transactions in 2022. In 2023, Houlihan Lokey generated an average of more than $4.1 million of revenue from each restructuring deal.

Why Now Is the Time to Buy HLI Shares

Bankruptcies and restructuring happen all the time, but when the economy falters, the countercyclicality of restructuring begins to shine. It happened in 2008, it happened in 2020, and as inflation and high interest rates stick around, it is happening again.

Today, we face a global synchronized "**Minsky Moment**" – a period of financial instability, as high inflation forces central banks to replace the cushion of easy money with the most aggressive monetary tightening campaign in a generation.The world's economy is on the precipice of a debt crisis unlike any that's ever happened before.

Even as the Fed begins lowering interest rates, the impact of the previous rate hiking cycle will be felt for years to come. The costs for businesses to borrow money will remain higher for longer, with S&P Global estimating that higher corporate interest expenses will result in an additional $8.6 trillion in debt servicing costs over the next few years. These higher costs have already started to cause a persistent rise in defaults, which will continue growing over time.

HLI's earnings from restructuring have already increased by 33% from 2022 to reach $522 million in fiscal year 2024. If bankruptcies surge again like they did after the dot-com bubble, the financial collapse of 2008 and the Covid-19 pandemic, restructuring revenue for HLI is set to accelerate over the next year. (Keeping in mind this business segment generated $600 million in revenue during the short-lived Covid crash, that's a conservative preview of what's to come.)

HLI's corporate finance segment generated impressive growth during the bull market from 2013 - 2022, with revenues growing from $200 million to $1.4 billion.

Now, we expect the restructuring arm to take the lead from the coming wave of corporate bankruptcies. We expect HLI's restructuring segment revenues to grow from $522 million in fiscal year 2024 to upwards of $1 billion per year in 2025.

That's what puts HLI right at the center of **The Greatest Legal Transfer of Wealth in History**.

The Big Secret Behind T. Boone's Fortune

Viper Energy (Nasdaq: VNOM) is an oil and gas royalty company: the best business in the energy sector. Unlike oil and gas producers, VNOM never invests any capital searching for oil or drilling holes deep into the earth. Instead, it simply owns the land upon which other companies drill – and collects a percentage of the cash flow. That makes it one of the most capital efficient businesses you'll find anywhere, with 75% free cash flow margins. VNOM funnels its profits directly to shareholders, instead of back into the ground.

The best part of VNOM's business is its strategic partnership as the leasing arm of Diamondback Energy, which is one of the lowest-cost, fastest-growing producers in America's most prolific oil basin: the Permian. Diamondback's low-cost leadership allows it to keep production growth going even when prices are low. That's a big reason why VNOM can keep its royalty volumes growing even during recessions and market crashes. This includes during the 2020 outbreak of the COVID-19 pandemic, when the global economy ground to a halt and oil prices fell to a record low of negative $40 per barrel. While most oil producers slashed production during the pandemic, VNOM's royalty volumes didn't skip a beat and instead grew by 23% in 2020.

VNOM has grown its royalty volumes every year since going public in 2014, regardless of the booms and busts in oil prices along the way. And this growth shows no signs of stopping, with royalty volumes increasing by 21% over the last 12 months, leading to new highs in VNOM's revenue, profit, and free cash flow. We're confident the company will continue growing its royalty volumes through the upcoming recession, just as it has in the past. Plus, VNOM trades cheap at less than 12x free cash flow. And its highly capital efficient business model allows the company to return a lot of its cash flow to investors, including a generous dividend yield of 5.5%.

The Big Secret Behind T. Boone's Fortune

In 1979, T. Boone Pickens created the first publicly traded "MLP" – a publicly traded partnership – that would own only mineral rights. He took most of the proven assets of Mesa Petroleum – huge oil and gas fields in Kansas, New Mexico, Colorado, and Wyoming – and he spun them off into a separately listed partnership, the Mesa Royalty Trust (NYSE: MTR, $16).

The idea was to separate the income streams from proven and operating fields from the costs of finding and developing additional fields. Doing so was much more tax efficient, as partnerships are not taxed like corporations are. Creating the trust meant shielding most of Mesa's income from corporate taxes. Mesa Petroleum, meanwhile, could take the capital from selling the assets, and continue to explore and develop more fields, activities that would generate tax-losses.

This structural innovation turned T. Boone into a "corporate raider" – as he couldn't figure out why much larger oil companies, like Gulf Oil, didn't do the same thing: Create royalty trusts to shield their income from taxes. T. Boone bought nearly 10% of Gulf Oil and demanded these changes be made, or else. The company was "in play" and through a series of mergers became Chevron. T. Boone made over $700 million on the investment for his partnership in two years' time.

Since those days, MLPs (master limited partnerships) have become a major segment of the stock market. They provide tax-efficient income for energy investors, much like REITs do for real-estate investors. Investing in the sector is tricky, however, as these partnerships normally have tax special accounting requirements. The good news is that's not a concern here. This company originally went public as an MLP in 2014, but then converted to a regular corporation in November 2023. This means investors can buy and sell the shares just like any traditional stock, without worrying about filing extra paperwork during tax season.

The MLP we're discussing in this section is **Viper Energy (VNOM)**.

The company's assets were developed by Diamondback Energy Inc. and are in the heart of Texas' leading field, the Permian Basin. But now these proven assets are owned by Viper Energy. If an oil company – Diamondback or anyone else – wants to produce oil from land that Viper owns mineral rights on, it must get Viper's permission. That means striking a deal where Viper extends a lease for the development of the resource in exchange for a cut of the profits.

T. Boone created the first energy trusts for tax reasons, but the advantages of these kinds of businesses go well beyond tax benefits. The key to understanding these businesses is that they don't have to pay any of the production costs or take any of the developmental risks: Viper just owns the mineral rights. The only cost Viper incurs is the upfront acquisition of the mineral rights. Once it owns them, all capital and operating expenses lie with the operator.

And that means, as inflation continues to drive energy prices higher, the rights that Viper acquired in the past become more and more valuable.

Viper transforms a capital-intensive industry into a capital-efficient business that's virtually guaranteed to produce increasing returns across time. In fact, Viper really isn't a business at all: it's mainly a legal fiction that generates enormous wealth. Well-run mineral rights businesses like Viper are truly one of Wall Street's greatest secrets.

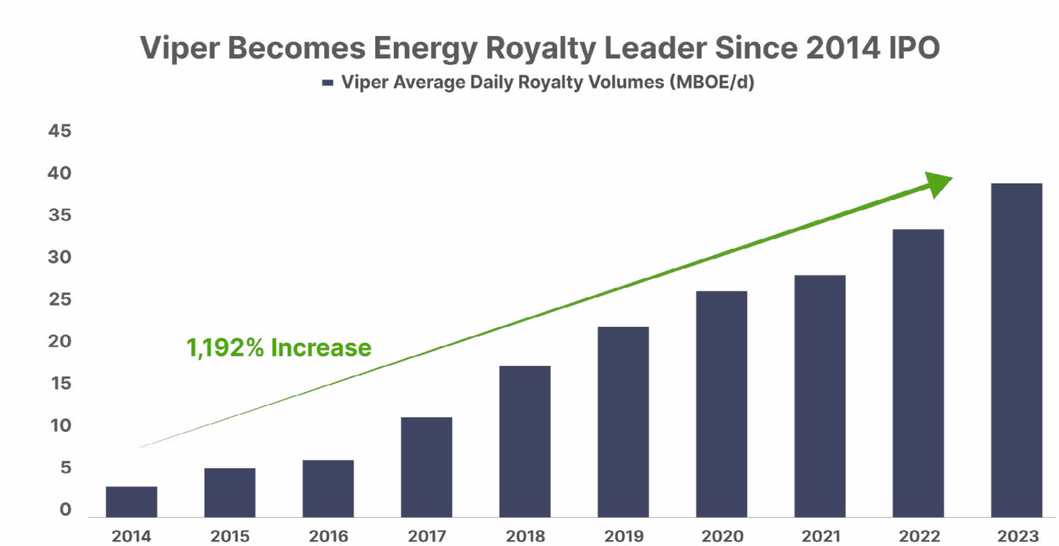
Consider: our standard rule of thumb when seeking out capital-efficient companies is finding businesses capable of converting at least 10% of sales into free cash flow, or a 10% free cash flow margin. **Over the last five years, Viper has averaged an incredible 75% free cash flow margin**.

Another metric of capital efficiency we look for are businesses that can earn $500,000 or more in operating income per employee. Well, Viper pushes the theoretical limit here. **The company has zero employees. You read that right – zero**.

Zero capital expenditures and zero employees make Viper one of the most capital efficient businesses in the entire stock market. But before explaining how this unique business model churns out gobs of cash with zero overhead, let's begin with the company basics.

Viper was one of the first pure-play energy royalty businesses in the Permian and leads the market in consolidating royalty acreage – investing over $2.5 billion acquiring mineral rights over the last several years.

Since going public in 2014, Viper's royalty volumes have grown nearly 12-fold, from average daily volumes of 3,000 barrels of oil equivalent (BOE) to 39,000 by the end of 2023:



Investors have reaped the benefits, with Viper shares outperforming the broader energy sector by a factor of 6 to 1 since its inception as a public company.

Viper owns mineral interests spanning across 34,217 net acres and over 9,000 producing wells, with net production of 39,244 barrels of oil equivalent per day ("BOE/d"). The company's total proven reserves stood at 179 million BOE as of year-end 2021, including 54% oil and 46% natural gas and natural gas liquids ("NGLs").

This reserve mix provides us with hedged exposure to a general bull market in fossil fuels – including oil and natural gas.

But more important than the what is the where. You see, the value of mineral rights goes beyond the cash flows that the existing oil or gas wells produce today. The real upside comes from buying the right acreage that has substantial upside from additional development in the future.

America's Greatest Natural Resource

Viper's asset base is concentrated in the heart of the Permian – America's most prolific oil and gas deposit. The Permian spans across 75,000 square miles in West Texas and New Mexico, and it's one of the oldest producing formations in America.

Unlike its next two closest peers – the Eagle Ford and the Bakken, which only sprang to life during the last decade's shale revolution – the Permian has produced oil and gas since the 1920s. The depth and quality of reserves are simply unmatched, as we can see in the data.

During each of the previous oil bear markets, including 2016 and 2020, the Permian suffered a shallower decline and faster recovery compared with the Eagle Ford and Bakken. And only the Permian has reclaimed new highs in output during each subsequent recovery, compared with the Bakken and Eagle Ford, which both remain below their production peaks reached back in 2014.

Going beyond oil, the Permian also hosts one of America's largest deposits of low-cost natural gas. Over the last decade, explosive growth in gas production has pushed the Permian into America's second-largest gas basin, trailing only the Marcellus formation in the Appalachian shale.

Finally, even more important than the what and where is the who.

Powerful Partnership

Viper's biggest edge comes from its strategic partnership with Diamondback Energy (NYSE: FANG), one of the best operators in the Permian, operating more than half of Viper's acreage.

Diamondback was ahead of its time with a concentrated focus on the Permian from day one, starting with over 4,000 acres in 2007 and expanding from there.

Because Diamondback began leasing up the Permian years before the shale boom, the company secured a leading acreage position that paved the way for incredible growth in oil and gas production over the last decade.

Meanwhile, management is among the best in the business, maintaining a disciplined approach to capital allocation and a conservative balance sheet. That's how Diamondback posted consistently impressive growth through the ups and downs in energy prices over the last decade.

In an industry that largely destroyed shareholder capital during the last decade, Diamondback became one of the best-performing stocks – not just in energy, but in the entire stock market. Shares have compounded at an incredible rate of 25% since going public in 2012, handily outperforming the energy sector and the overall stock market.

And this is great for Viper...

Diamondback is the majority owner of Viper, holding 54% of all outstanding units. This aligns Diamondback and Viper's incentives, ensuring that both parties profit from Viper's success. And it's this relationship that makes Viper's unit economics so compelling. Diamondback allows Viper to draw upon its internal staff and resources to the point where Viper requires zero of its own employees.

We can see clear evidence of the success of this model through Viper's track record of growing oil and gas reserves since inception, which has grown 9-fold from 19 million BOE in 2014 to 179 million at the end of 2023.

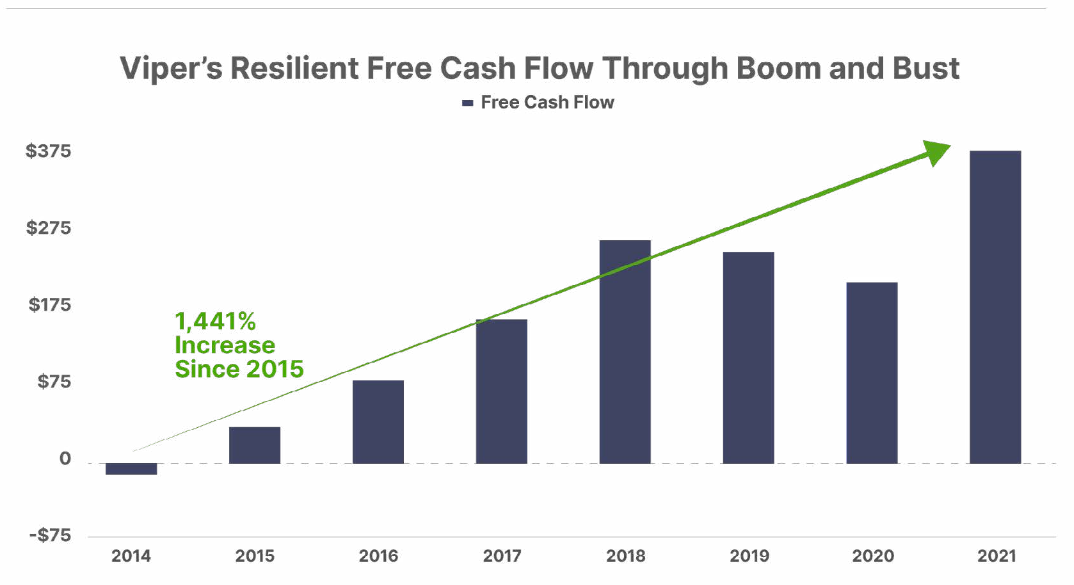
Viper is simply the publicly listed portion of Diamondback's huge royalty book. It allows investors to buy hydrocarbons directly, without the risks and capital requirements of production. In that way, Viper is more like a financing company than an energy company.

A Uniquely Safer Bet

Viper's unique business model offers remarkable resilience against the inherent volatility of oil and gas prices.

This is another feature of the company's capital efficiency. The cash flow statements for most commodity producers plunge deep into negative territory during commodity bear markets because the prices of the things they sell goes down, while operating costs and capital expenditures remain stubbornly high.

Viper's business model is designed to be immune from this defect. The following chart shows how Viper sailed through 2020 energy price collapse with barely more than a blip in its cash flow trajectory:



Take another look at the chart above. You can see how Viper is enjoying substantial upside from today's high-price environment... Free cash flow is surging, thanks to the combination of higher prices on its royalty volumes along with its longer-term trend of volume growth.

In other words, Viper provides all the upside from higher energy prices, with only a fraction of the downside compared with traditional oil explorers and producers.

For such a compelling business model, you would expect Viper to command an exorbitant valuation premium. And yet, with a market capitalization of $8.2 billion, the company trades at less than 12x free cash flow today.

The best part? Without needing to recycle earnings back into expensive equipment and other operating costs, that cash flows right back to investors. That's how the company pays out a current annual dividend of $2.56, or a yield of 5.5%

Of course, if energy prices fall, so, too, will the company's cash flow – and the distribution. Plus, because Viper is technically an "energy" company, the share price can fluctuate wildly, along with the overall volatility in the energy sector.

That's why anyone owning these shares should be able to separate short-term market volatility from the true risks in the underlying business. For all the reasons we've discussed today, we view Viper as one of the lowest-risk businesses in the energy sector. No capital requirements, no operating costs, high and stable cash flows (even during energy bear markets), and a clean balance sheet.

In terms of business risk, you can't do much better... in energy or elsewhere in the market.

A note from Porter:

I hope you've enjoyed these six stock stories... and that you'll find them useful as we move closer to the inevitable recession.

Each one of these stories first appeared in one of my member publications at Porter & Co. However, the versions you see here have been edited and condensed, because (unlike END OF AMERICA) I didn't want to make this report 91 pages long.

The full versions of these writeups, along with all my other research and recommendations, can be found on the **Porter & Co. members' website**.

Porter Stansberry
Stevenson, MD