Porter & Co.

THE BIG SECRET ON WALL STREET

The Two Resource Royalty Gold Mines

- The Gold Digger That Gets Paid To Do Nothing
- Owning The Energy, Not The Production Costs

FROM THE DESK OF PORTER STANSBERRY

SPECIAL REPORT

The Two Resource Royalty Gold Mines

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Let us introduce you to the wonderful world of resource royalty companies.

Royalty companies are some of our favorite – and somewhat off-the-radar – capital-efficient companies at Porter & Co.

These firms raise capital and then invest in operating businesses. But rather than buying stock or lending on credit, they simply buy a small percentage of the operating company's future revenue. This allows royalty companies to share in the business' success without bearing the operational risks or capital costs of actually operating the business.

Royalty companies are a great way to invest in almost any industry or trend. But they're the absolute best way to invest in the resource sector. That's because producing commodities is generally a terrible business.

Consider the case of gold mining. While gold is one of the most valuable commodities on the planet, very few companies can consistently earn profits from mining over the long run.

Gold mining requires a lot of upfront capital for exploration, development, and construction. This capital is often tied up for a decade or longer before a mine produces any revenue.

But it doesn't get any better once a mine is operating.

Digging miles into the Earth to extract physical gold is also capital intensive. A substantial portion of profits must go back into the ground to keep production going and continuously replace the depleting asset base of existing mines.

Mining companies spend enormous sums on labor, capital, and finding new reserves – money that doesn't go to shareholders. And along the way, economics can change drastically due to the cyclical nature of commodity prices.

It's a similar story in virtually every other resource business, from copper mining to oil and gas production.

For example, drilling shale wells is like running on an endless treadmill; as soon as a well comes online, production begins rapidly depleting. This means a big chunk of the profits from existing wells must constantly go right back into the ground to drill more wells to keep production growing.

These investments create a lot of risk, as oil and gas prices are incredibly volatile. And the capital required significantly reduces the amount of profit that eventually reaches investors, especially if it is invested unwisely or even just at the wrong time.

As Warren Buffett's longtime right-hand man Charlie Munger once explained:

> *"There are two kinds of businesses. The first earns 12%, and you can take it as cash. The other earns 12%, but all must be reinvested. It reminds me of the guy who looks at his equipment and says, 'There's all of my profit.' We hate that business."*

Resource royalty companies avoid this trap. They essentially let other people do the hard work of mining or drilling for them. The other folks put in the long hours and do the tedious and expensive legwork of exploration and production, while the royalty company simply sits back and reaps the benefits.

In this report, we're about to show you the details of two of our favorite resource royalty firms... capital-efficient companies that will compound your money as America's Resource Renaissance takes hold, without the risks of investing in commodity producers directly. As a bonus, we've added a writeup on a third royalty company that trades at an attractive valuation multiple of less than 10x earnings, and pays out a juicy 11.6% dividend yield.

The Gold Digger That Gets Paid To Do Nothing

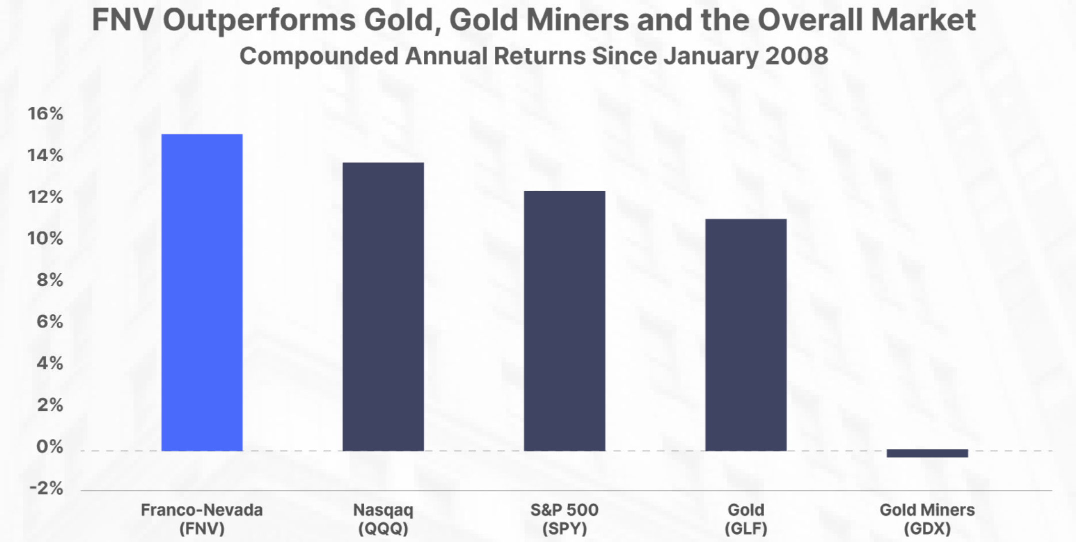
Franco-Nevada (NYSE: FNV) is a gold royalty company headquartered in Toronto, Ontario.

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 $1.1 billion in revenue in 2024 and $493 million in net income.

That's more than $10 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 2024, FNV generated $421 million in free cash flow for a 38% free cash flow margin. As a frame of reference, that's well above the 30% free cash flow margins of Microsoft – one of the best businesses in the world – and on par with the rest of the mega-cap tech cohort that has led the market in recent years. It also beats the free cash flow margins of the world's two top gold miners, Barrick Gold (11%) and Newmont (16%).

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, with no additional costs incurred by FNV.

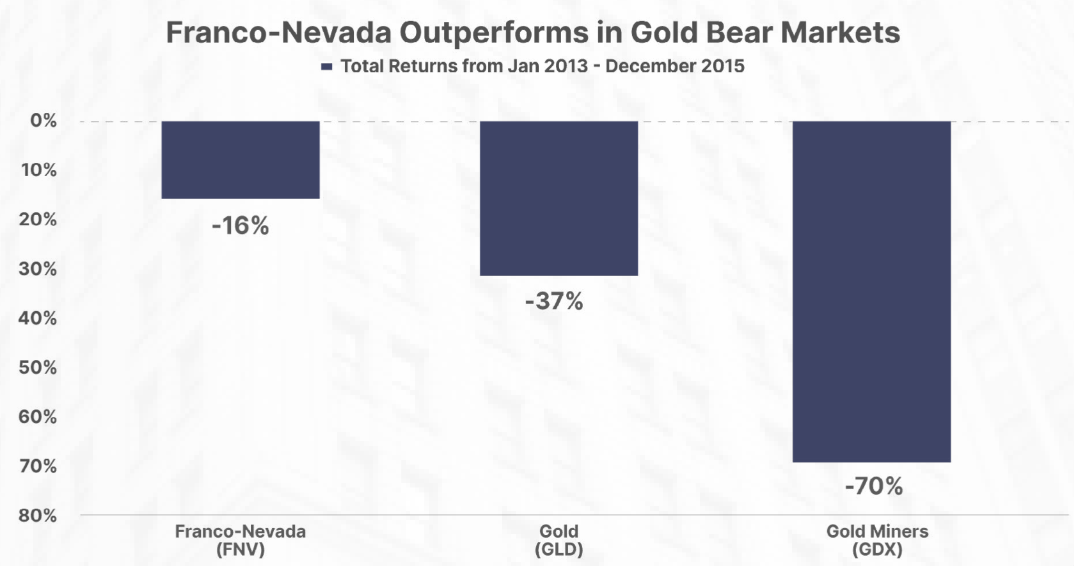
And that's where FNV's business model really shines. FNV strikes deals designed to recoup its original investment plus a double-digit rate of return while retaining future upside in perpetuity.

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.

The Lower-Risk Way To Invest In Gold

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.

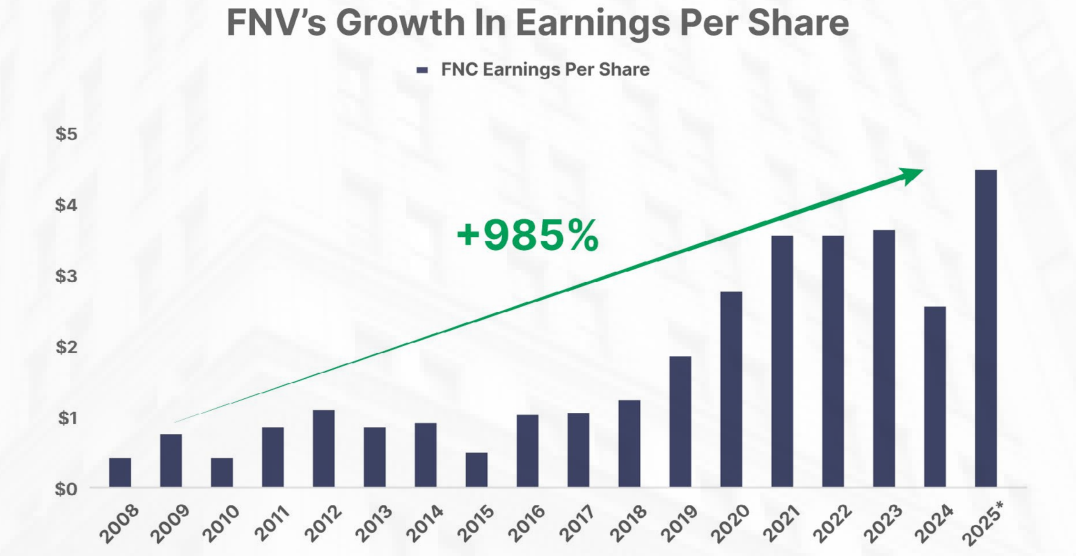
The final downside protection in FNV's capital-efficient business model comes from the company's ability to fund most of its growth through free cash flow, avoiding the risk of taking on excess debt.

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 $1.1 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 2024. And the return on that capital raised has been spectacular.

Since 2008, FNV has increased its net income from $40 million to a projected $892 million this year, based on Wall Street analyst estimates. Over the same period, earnings per share have soared 10-fold, from $0.41 in 2008 to a projected $4.45 this year:



2025& Based on Analyst Estimates

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.

Action to Take: For the latest updates on our open positions and current buy up to prices, please visit our live portfolio **here**.

Owning The Energy, Not The Production Costs

Viper Energy (Nasdaq: VNOM) is one of the world's best energy royalty companies.

The company's assets were developed by shale driller Diamondback Energy Inc. (NYSE: FANG) and are in the heart of Texas' leading oilfield, the Permian Basin. In 2014, Diamondback created Viper Energy as a separate company to own and manage these properties. Through this transaction, Viper became a separate publicly traded entity, although Diamondback retained a controlling interest, and today owns 56% of Viper's shares (more on this later).

Since Viper now owns these properties and the associated mineral rights, this means that if an oil company – Diamondback or anyone else – wants to produce oil from land that Viper owns, 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.

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.

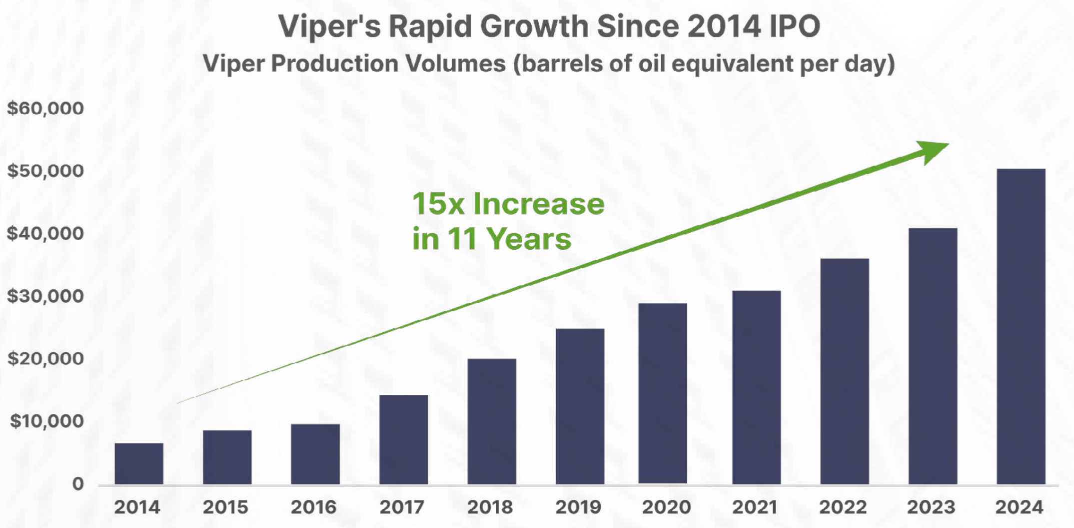
Consider: our standard rule of thumb when seeking out capital-efficient companies is finding businesses capable of converting at least 10% of sales into free cash flow, or a 10% free cash flow margin. Over the last five years, Viper has averaged an incredible 75% free cash flow margin.

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.

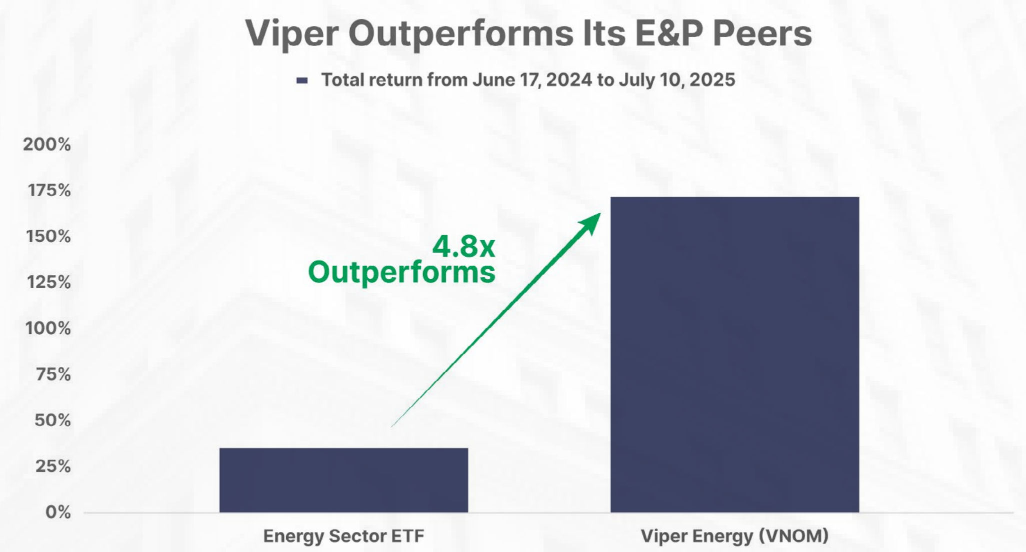
Zero capital expenditures and zero employees is how Viper offers one of the most capital-efficient businesses – not just in the shale patch – but in the entire stock market. But before explaining how this unique business model churns out gobs of cash with zero employees and zero capital expenditures, let's begin with the company basics.

Viper was created as a spin-off from Diamondback Energy in 2014. 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.

In the 11 years since it went public in 2014, Viper's royalty volumes have grown 15-fold, from average daily volumes of 3,000 barrels of oil equivalent ("BOE") to 49,000 in 2024:

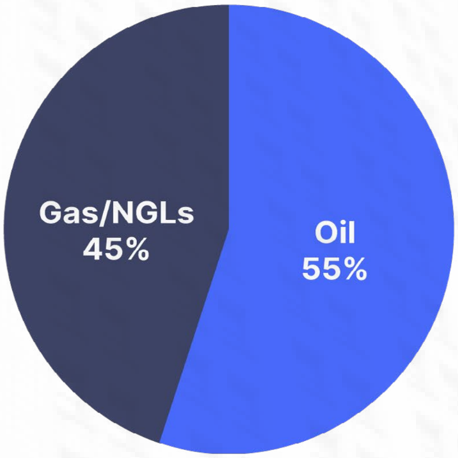


Investors have reaped the benefits, with Viper shares outperforming the broader energy sector (measured by the SPDR Energy Sector exchange traded fund) by a factor of 4.8 to 1 since its inception as a public company in June 2014:



Viper owns mineral interests spanning across 1.2 million gross acres and 15,000 producing wells, with net production of 49,000 barrels of oil equivalent per day ("BOE/d"). The company's total proven reserves stood at 179 million BOE as of year-end 2023, including 55% oil and 45% natural gas and natural gas liquids ("NGLs"):

Viper's Reserves by Component



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

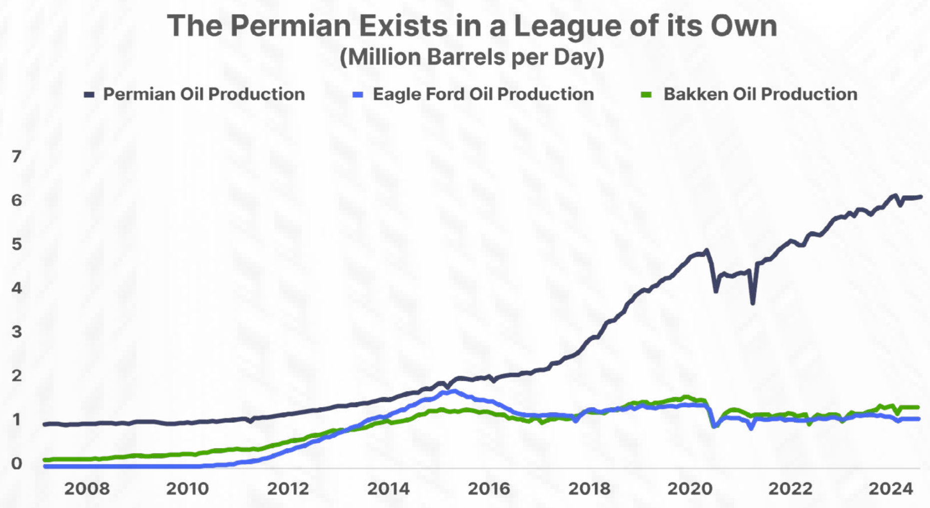
But more important than the what is the where. You see, the value of mineral rights goes beyond the cash flows that the existing oil or gas wells produce today. The real upside comes from buying the right acreage that has substantial upside from additional development in the future.

Buy The Permian, Now

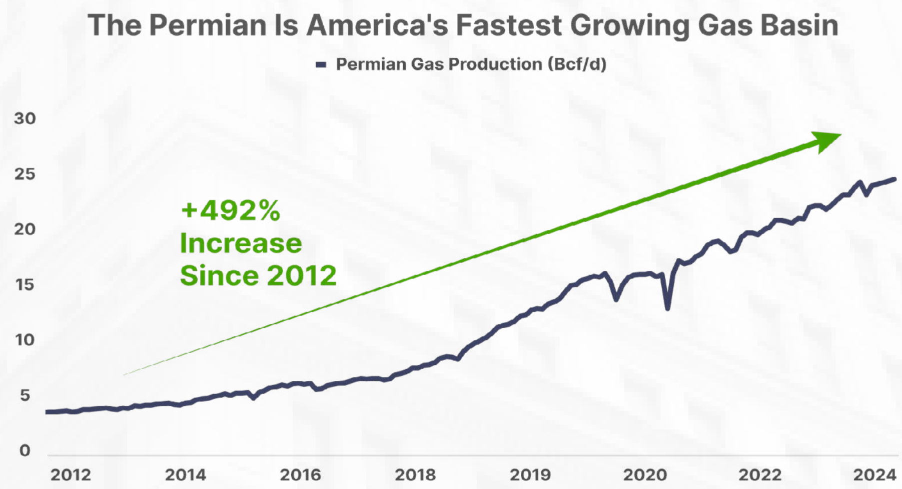
Viper's asset base is concentrated in the heart of the Permian – America's most prolific oil and gas deposit. The Permian spans across 75,000 square miles in West Texas and New Mexico, and it's one of the oldest producing formations in America.

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, the Permian has become America's fastest growing gas basin, with a remarkable 492% increase in production since 2012 (it's now the second-largest US gas basin by production, trailing only the Marcellus formation in the Appalachian shale):



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

Powerful Partnership

You see, owning mineral rights on great acreage is only half the battle. After all, mineral owners only get paid when oil and gas gets produced. That's why it's critical to partner with the right operators to maximize the value of that acreage.

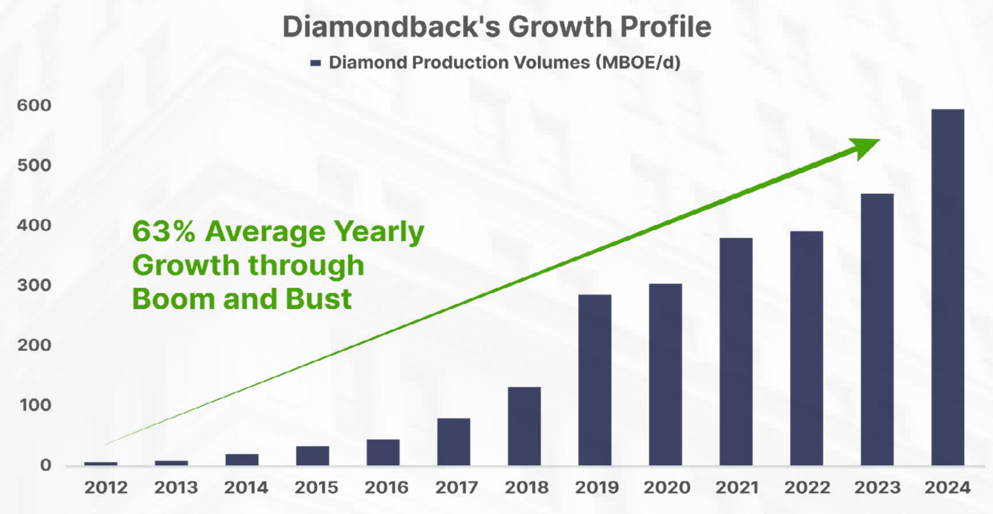
And that's where Viper's biggest edge comes from, through its strategic partnership with Diamondback Energy, one of the best operators in the Permian, operating more than half of Viper's acreage.

Diamondback was formed in 2007. Back then, T. Boone Pickens and just about everyone else believed that the Permian's best days were behind it… and for good reason. For the previous 35 years, production entered into secular decline, from a prior peak of 2.2 million barrels per day (b/d) in 1972 down to a low of around 750,000 b/d in 2008.

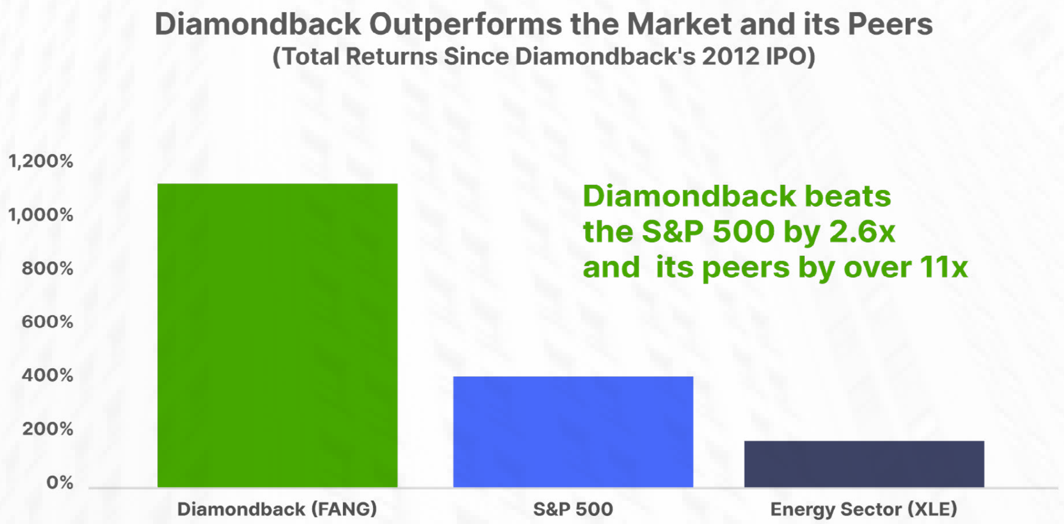
But operators like Diamondback, along with the new production and completion techniques of the shale revolution, brought the basin back to life. Today, the Permian is America's largest low-cost oil basin, producing over 6 million b/d.

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 averaging 63% per year since its 2012 IPO, through the ups and downs in energy prices along the way:



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 compounded at an incredible rate of 24% since going public in 2012, handily outperforming the energy sector and the overall stock market:



With record profits and production and more than a decade of tier-one inventory in the heart of America's top oil and gas basin, Diamondback's prospects look brighter than ever. This, in turn, is great for Viper.

That's because Viper enjoys a unique relationship with Diamondback, which unlocks tremendous capital efficiency in a way that we haven't found anywhere else in the shale patch.

Diamondback is the majority owner of Viper, holding 56% of all outstanding shares. 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.

Viper leans on Diamondback to identify the best Permian oil and gas acreage – something Diamondback has already done for the last 15 years and will continue to do going forward. Viper uses this information to strike deals that involve an upfront payment to acquire mineral rights on highly productive acreage.

We can see clear evidence of the success of this model through Viper's track record of growing oil and gas production inception, which has increased by 15-fold over the last 11 years.

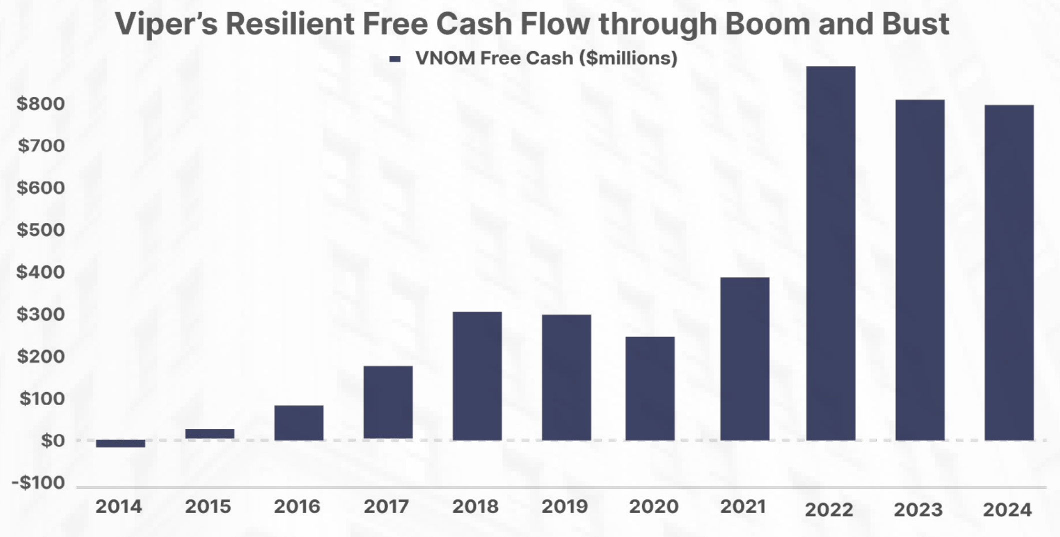
Viper is simply the publicly listed portion of Diamondback's huge royalty book. It allows investors to buy hydrocarbons directly, without the risks and capital requirements of production. In that way, Viper is more like a financing company than an energy company.

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 the post-COVID recovery in energy prices... Free cash flow has more than tripled from less than $200 million in 2020 to over $600 million in each of the last three years, 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 roughly $10 billion, the company trades at just 16x free cash flow. That's a nearly 50% discount to the S&P 500's valuation at 31x free cash flow.

Said another way, Viper's free cash flow yield (or the percentage of its free cash flow divided by its current market capitalization) is over 6% versus 3% for the overall market. And because of Viper's highly capital efficient business model, it can return most of that free cash flow to investors through a current dividend of $2.28per year, or a yield of 6%.

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

That's why anyone owning shares in Viper 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 employees, and high and stable cash flows that remain resilient even during energy bear markets. Best of all, this is a business built to consistently return its high (and growing) free cash flow to investors through steady dividend payments.

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

Action to Take: For the latest updates on our open positions and current buy up to prices, please visit our live portfolio **here**.

Porter Stansberry

Porter & Co.
Stevenson, MD

P.S. If you'd like to learn more about the Porter & Co. team, you can get acquainted with us **here**. You can follow me (Porter) on **X** here: **@porterstansb**