Big Gold

Casey Research

Big Profits from the Gold Bull Market

Volume III, Issue 2 / February 2011

Royalties Happen

Metals Prices				
Resource	**Last**	**1 Month Ago**	**3 Months Ago**	**1 Year Ago**
Gold	1,363.80	1,378.75	1,388.50	1,082.00
Silver	30.20	29.22	26.79	15.33
Platinum	1,355.00	1,793.00	1,712.00	1,505.00
Palladium	827.00	803.00	703.00	416.00
Copper	4.51	4.40	3.75	3.09
Nickel	12.72	11.71	9.90	8.35
Zinc	1.10	1.11	0.97	0.98

In This Month's Issue…

Click on the link to jump directly to an article.

Dear Readers,

Does the decline in the gold price have you worried?

Gil [name changed] wrote last week saying he was concerned about gold's retreat this year. His worry was that the price has been mostly a one-way ticket down: by the end of January, gold had fallen 6.6%, the biggest drop for that month in 20 years. So, should we be concerned?

Longtime readers probably know how we feel about such things, but we did a quick analysis of the correction to see how it measures up…

Gold Correction Diagnosis: Normal

If I analyzed the gold market the way a physician would evaluate a patient's complaints, I would come to one conclusion: there's nothing wrong. The results of the testing are normal.

First, from a price perspective, gold ended 2010 with an 18.5% run from its summer low on July 28. So a pullback here is natural and even expected. And as we stated last month, when gold enters a correction phase, the average decline is 12.8% (of those greater than 5%). A 12.8% pullback from the year-ending high of $1,421.60 would take us to about $1,240. Our current decline is thus less than average.

Second, from a seasonal perspective, gold is following its usual pattern. The annual low has occurred in January or February in six of the last 10 years, and by May in every year but one. So it's behaving as it typically does this time of year.

Even if the gold price were to end up lower at the end of the year, it wouldn't mean the bull market is over. Gold fell 50% over a two-year span during its greatest bull market in history (1970-1980). It's fallen 27.7% *twice* in the current bull market and yet later soared to new highs. To be clear, we're not expecting a decline of these magnitudes, but it does demonstrate that the price on any given day doesn't always reflect the big picture.

Third and most important are the fundamental factors driving the bull market. Are they still intact?

- U.S. debt? Beyond repair and still rising.
- Sovereign debt issues? Unsolved for many countries.
- Government M.O.? Still printing enormous amounts of money, particularly in the U.S.
- Politicians? Still spending more money than they have.
- Real interest rates? Still negative.
- The risk to the U.S. dollar? Severe. Potentially life-changing.
- Inflation? Officially low, but food and commodities are up and destined to climb higher.
- Economic woes (unemployment, bank closures, real estate, etc.)? No letup in sight.
- Middle East? Up in flames.
- N. Korea? Still rattling sabers.
- Gold production? Relatively flat in spite of much higher metal prices.
- Total gold supply? Remains tight in spite of increased scrap coming to market.
- Gold demand? Unrelenting for physical metal.

The conclusion to draw from all these factors and more is unchanged: gold remains in a bull market and a must-own asset. *Not until these factors reverse will we reconsider our focus on precious metals.*

The bottom line, Gil, is that this is normal price behavior. Keep the big picture in mind, and don't fret the inevitable gyrations along the way. In fact, there's a fair chance we could be nearing the low for the year. If you're a contrarian investor, and even if you're not, you might consider this an opportunity to add the one asset to your portfolio that can't fall prey to the three D's: dilution, debasement, and devaluation. *No matter what governments do, the gold you purchase today will buy you the same amount of goods and services in the future.*

BIG GOLD Buyer's Box

→**Franco-Nevada (T.FNV),** this month's new stock pick. See our write-up and specific recommendations below.

→**Gold and Silver**

Best Buy: The lowest premium right now for a one-ounce gold bullion coin is the Canadian Maple Leaf, including the Olympic version. At Kitco, for example, it's about $20 cheaper than the Eagle, $67 below the Buffalo, and $13 less than the Philharmonic (though you may find them even cheaper at our other dealers).

Check prices at your local shop, or try one of our recommended dealers:

Milesfranklin.com; 1-800-822-8080
Thecoinagent.com; 1-888-494-8889
Bordergold.com; 1-888-312-2288
Kitco.com; 1-877-77-KITCO (775-4826)
Tulving.com (large orders); 1-800-995-1708
Assetstrategies.com; 1-800-831-0007

(For gold and silver funds, see the portfolio table below.)

→**Precious Metal Stocks.** The correction has made many of our positions great buys if you intend to hold to the end of the bull market. Even better prices could be ahead; here's our updated recommendations for the next 30 days (remember, one tranche at a time):

Stock	Updated Recommendation
Alamos Gold (T.AGI)	Buy 1 tranche at or <$16
Agnico-Eagle (AEM)	Buy 1 tranche at or <$68
Barrick (ABX)	Buy 1 tranche at or <$46
Eldorado (EGO)	Buy 1 tranche at or <$16
Kinross (KGC)	Buy 1 tranche at or <$16
Minefinders (MFN)	Hold
Randgold (GOLD)	Hold
Royal Gold (RGLD)	Buy 1 tranche at or <$46
Silver Wheaton (SLW)	Buy 1 tranche at or <$30
Silvercorp (SVM)	Buy 1 tranche at or <$10
Yamana (AUY)	Buy 1 tranche at or <$11

Are we buying now? Yes, some, but we're not draining our cash accounts to do so. In other words, leave some money aside in case we see further price weakness.

We're also buying a new stock this month, one we think is one of the safest gold investments you can make. It's a great buy-and-hold asset for the gold bull market. Check out our recommendation below, including our interview with the chairman. I'll be tucking away a few shares myself once it hits our price target.

There are times to buy and times to refrain from buying. Unlike last fall when gold and gold stocks were soaring, we think we're nearer the time to buy.

TOP

Royalties Happen

Wouldn't it be keen to own a small part of a gold mine and get paid a percentage of the value of the metal they sent to the refinery? And let's say as part owner, you absorbed none of the expenses to mine the metal, and in fact, were paid regardless of what it cost to extract the gold. You simply receive checks, cash them, and wait for the next one.

That's the job description of a royalty holder.

Even better would be to own dozens of royalties – and better still would be to have someone manage it all.

That's the job description of a royalty company.

Now *that's* anattractive investment. Let's take a closer look at how royalties work, which will demonstrate why we're adding one of the top gold royalty companies to our portfolio…

In its simplest form, a royalty entitles the holder to a fixed percentage of all the specified minerals produced from a given deposit. The entitlement isn't usually subject to a time limit – most continue for as long as there's production. And the holder of a gross royalty doesn't pay any share of the cost of producing the minerals – it gets its cut right off the top, before expenses or taxes.

A royalty can be granted anywhere in the process of turning dirt and rock into a mine. A prospecting company, for example, might acquire the rights to mine a particular area by paying the landowner a little cash and promising a royalty on whatever actual production occurs. Or a mine developer might sell a project to a bigger company but retain a royalty. Or, much later in the game, a mining company might sell a royalty to an investor to raise the cash needed to go into production.

> The accounting for a royalty is usually tied to the refining of the ore, and that's where the variations on the royalty concept begin. The two most common agreements are a Gross Smelter Return (GSR) and Net Smelter Return (NSR). A GSR royalty is a percentage of the gross revenue reported by the smelter. An NSR royalty, on the other hand, is reduced by a proportional share of the miner's costs of getting the smelting done – transportation, insurance, refining, and charges by the smelter. In the case of gold, the difference isn't usually much, roughly $2 an ounce.

Once a royalty has been created, it assumes a life of its own. It remains attached to the property, like a mortgage, even if the property changes hands. And the royalty owner can sell it, in much the same way any other property is sold.

As you might suspect, whether you're a potential buyer or seller, valuing royalties isn't simple. How much, if any, production there will be, how rapidly the mineral will be produced, and what price it will fetch when it comes out of the ground are among the uncertainties that can't be eliminated and must be weighed.

Doing the weighing requires the knowledge of a mining engineer, the understanding of an economist, and the instincts of a bookmaker. And we've found a company that is tops in doing all that – and was, in fact, the originator of the gold royalty concept.

TOP

Franco-Nevada: The Original Gold Royalty Company

Franco Nevada HM: Au, Ag, Pt, Pd, Ni, Cu, Pb, Zn TSX.FNV, FNNVF.PK, www.franco-nevada.com			
Price	Share: C$29.19	MCap: C$3.34B	On 02/07/11
Shares	Est. SO: 114.5M	FD: 128.9M	As of: 12/30/2010
Warrants	UnEx: 11.5 M	C$32.00	Exp: March 13, 2012
		C$75.00	Exp: June 16, 2017
Options	Open 2.8 M	C$15.20 to C$31.45	
Debt	None		
Cash	Est. US$610M	EPS: US$0.16/share	As of: 12/30/2010

Buy One Tranche At or Under C$29. Franco-Nevada Corp was the first company to use the royalty model in the gold industry. FNV started in 1985, sold the business to Newmont in 2002, and then re-purchased the royalty portfolio in January 2008. What's attractive about FNV today is the pending buyout of Gold Wheaton (T.GLW), a smaller royalty company with some attractive gold and other precious metal assets. If approved by voters, FNV's royalty revenue will jump by a whopping 50% and make precious metals over 85% of total revenue, giving them considerable leverage to gold. Here's our 8 P's review…

People

Franco-Nevada is chaired by Pierre Lassonde, who many consider a leader in the gold industry. Pierre was president of Newmont Mining from 2002 to 2006, and co-founder and co-CEO of the original Franco-Nevada from 1982 to 2002. He is past chairman and a current director of the World Gold Council, author of *The Gold Book*, has served on many mining boards and committees, and won numerous industry awards. See our interview with him below.

President and CEO is David Harquail, who also hails from Newmont Mining, as well as the original Franco-Nevada. Like Pierre, he has served on numerous mining boards and industry associations.

Heading up acquisitions is senior VP Paul Brink, with experience in mining-focused investment banking and financing at Newmont Capital, BMO Nesbitt Burns, and UBS.

There are many other key executives with the company, which you can see here and here. All told, this is a highly experienced team with over a century of combined experience.

Properties

If the acquisition of Gold Wheaton goes through – probable, but not guaranteed – Franco-Nevada will have a total of 35 producing royalties (currently 32), 29 of which will come from precious metals (currently 27). While the company has over 100 oil and gas concessions, revenue from precious metals currently comprises 83% of income, which will increase to 85% post-buyout (86% on a NAV basis). And 82% of precious metal revenue will come solely from gold. At that point, Franco-Nevada will be earning a higher percentage of revenue from precious metals than Royal Gold.

Here's a list of the company's current royalties.

Franco Nevada Royalties

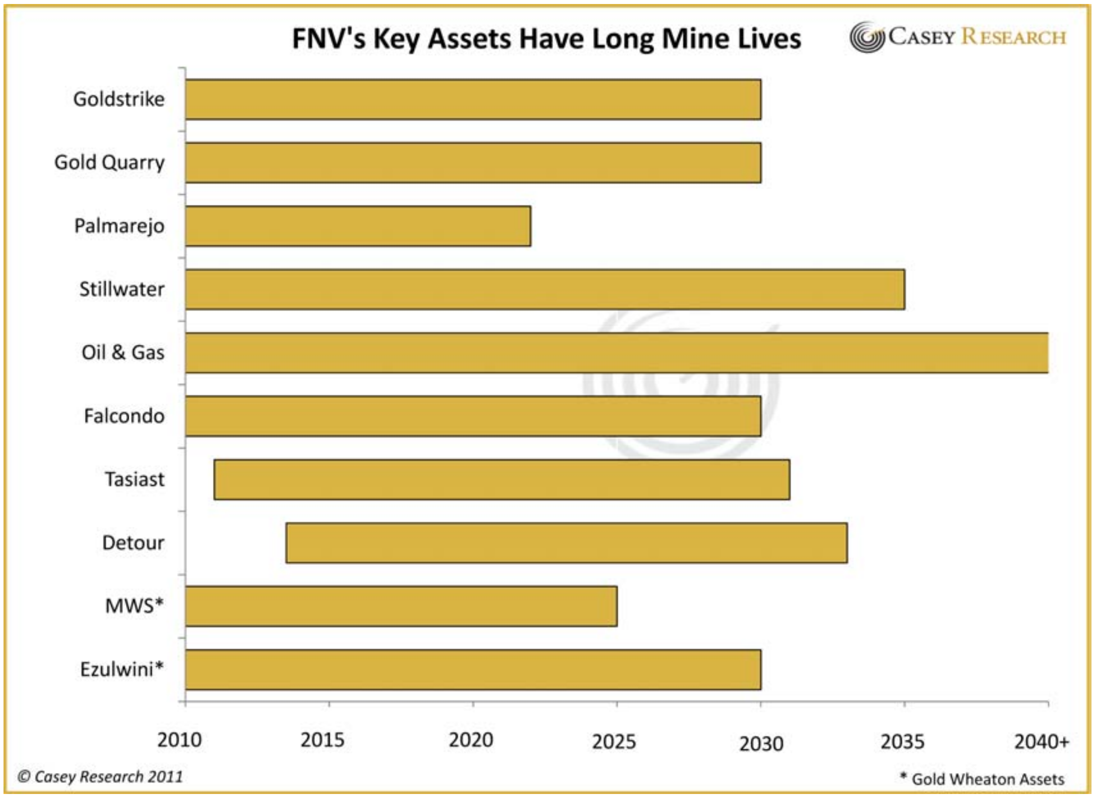
Mine	Operator	Location	Royalty %	Royalty Terms	Royalty Revenue Q310 ('000s)
Gold					
Goldstrike	Barrick Gold	Nevada	2-4%	NSR	4,521
Goldstrike	Barrick Gold	Nevada	2.4-6%	NPI	11,691
Palmarejo	Coeur d'Alene Mines Corp	Mexico	50%	Gold Stream	12,396
Gold Quarry	Newmont	Nevada	7%	NSR	1,392
Marigold	Barrick Gold / Goldcorp Inc.	Nevada	1.75-5%	NSR	1,402
Bald Mountain	Barrick Gold	Nevada	1-4%	NSR	288
Bronzewing	Navigator Resources Limited	Australia	1%	NSR	341
Cerro San Pedro	New Gold Inc.	Mexico	2%	GR	1,224
Henty	Bendigo Mining Limited	Australia	1-10%	ORR	602
Hislop	St. Andrew Goldfields Ltd.	Canada	4%	NSR	381
Hollister (Ivanhoe)	Great Basin Gold Limited	Nevada	3-5%	NSR	570
Holloway	St. Andrew Goldfields Ltd.	Canada	2-15%	NSR	1,300
Mesquite	New Gold Inc.	US	0.5-2%	NSR	758
Mouska	IAMGOLD Corporation	Canada	2%	GR	3
Mt. Muro	Straits Resources Limited	Indonesia	3-7%	NSR	334
New Celebration	Avoca Resources Limited	Australia	2%	NSR	289
North Lanut	Avocet Mining plc	Indonesia	5%	NSR	623
Robinson	QuadraFNX Mining Ltd	Nevada	0.225%-0.25%	NSR/Other	159
Platinum Group Metals					
Stillwater Complex	Stillwater Mining Company	Montana	5%	NSR	2,412
Pandora	Anglo American Platinum/Lonmin	South Africa	5%	NPI	N/A
Base Metals					
Mt Keith (nickel)	BHP Billiton Limited	Australia	0.25%-0.375%	NPI/GR	758
Robinson (copper)	Quadra Mining Ltd.	Nevada	0.225% & other	NSR & other	174
Commodore (coal)	Millmerran Operating Company	Australia	other	other	N/A
Eagle Picher (diatomite)	EP Minerals, LLC	Nevada	other	other	76
Kasese (cobalt)	Blue Earth Refineries	Uganda	other	10% FCF Share	25
Oil and Gas					
Edson	Canadian Natural Resources	Alberta	15%	ORR	1,920
Weyburn Unit	Cenovus Energy Inc.	Saskatchewan	0.441%-1.110%	ORR/WI	2,590
Midale Unit	Apache Canada Ltd.	Saskatchewan	1.175%/1.594%	ORR/WI	829
Other	Various	Various	Various	Various	2,049

**NPI/Net Profit Interest: profit realized after deducting costs related to production per royalty agreement. GR/Gross Royalty: based on total revenue from production with few if any deductions. ORR/Overriding Royalty: based on proceeds from gross production and usually free of any costs.*

Notice that many of the royalties are not negotiated at a fixed percentage rate. This is important, because a straight 3% royalty on a closed mine yields exactly 3% of nothing. An intelligent royalty holder wants to encourage the producer to keep the project up and running. "Sliding scale" royalties accomplish this by reducing the bite during hard times and increasing it during times of plenty.

To be clear, a mine with declining production will result in a reduced payment coming to the royalty holder. And Franco-Nevada, like Royal Gold and Silver Wheaton, have little control over how much mining will be done at a given project in a given time period; the operator makes the decisions about when, where, and at what pace all mining will take place. In a few cases, FNV has a royalty on only a portion of a project, meaning they're at the mercy of the producer as to when that section gets mined. While this could have some quarter-to-quarter impact on income, the model works very well when viewed over the life of a project.

Another important factor is how long a mine will be operating and thus paying the royalty holder. Mines are finite operations, so we want projects with long mine lives. Here's a measure of the longevity of FNV's key assets.



The chart shows that Franco-Nevada expects to collect royalties for the next 20+ years on its key assets.

The MWS and Ezulwini gold mines coming from Gold Wheaton are located in South Africa (see Politics below) and currently generate about $4 million and $3.3 million/quarter, respectively, in royalty revenue. The biggest attraction from the buyout is the Sudbury Footwall operation in Canada, which currently yields over $10 million/quarter in revenue from gold, platinum, and palladium. Sudbury is located in a world class mining district and has five deposits, one of which has significant resource upside. All told, revenue is projected to increase by as much as $100 million/year from the acquisition.

What about future royalties? Here's a list of royalties that have yet to kick in.

Future Royalties*				
Mine	**Operator**	**Location**	**Royalty %**	**Royalty Terms**
Mines Restarting Production:				
Falcondo	Xstrata	Dominican Republic	4.1% equity	Equity
Holt	St Andrew Goldfields	Canada	up to 10%	NSR
Royalties About to Kick In:				
Subika	Newmont	West Africa	2%	NSR
Ity	La Mancha	West Africa	1%	NSR
Hemlo	Barrick Gold	Canada	50%	NPI
Musselwhite	Goldcorp	Canada	5%	NPI
Pandora Platinum	Anglo Platinum/Lonmin	South Africa	5%	NPI
Projects Awaiting Permits:				
Rosemont	Augusta Resources	Arizona	2%	NSR
Perama Hill	Eldorado Gold	Greece	2%	NSR
Pre-feasibility Stage:				
Sandman	Newmont/Fronteer Gold		0.5 – 5%	NSR
Garden Well	Regis Resources	Australia	2%	NSR
Goldfields	Brigus Gold	Canada	2%	NSR
Courageous Lake	Seabridge Gold	Canada	1%	NSR
Gurupi	Jaguar Mining	Brazil	1%	NSR
Mara Rosa	Amarillo Gold	Brazil	1%	NSR
Agi Dagi	Alamos Gold	Turkey	2%	NSR
Kiziltepe	Ariana	Turkey	1.5 – 2.5%	NSR
Mines Starting Production <1 year:				
Duketon	Regis Resources	Australia	2%	NSR
Lounge Lizard	Kagara Ltd	Australia	2%	NSR
Red October	Saracen	Australia	2%	NSR
Tasiast	Kinross	West Africa	2%	NSR
Detour Lake	Detour Gold	Canada	2%	NSR

**Mine lives have not been determined for all mines; exploration is ongoing at most projects.*

The potential revenue from these additional royalties *exceeds $2 billion*, and that's without further exploration and discoveries. In fact, by 2015, annual royalty revenue is expected to be more than twice that of 2010, reaching $350 million or more. And all this will transpire with minimal exposure to rising costs, something we expect will pinch producers harder and harder as inflation inevitably rises. If you're bullish on the price of gold, it's easy to see how this company can earn enormous profits over the coming years.

Politics

Currently, 95% of the company's royalties come from operations in Canada, Mexico, U.S., or Australia, locations we consider relatively safe mining jurisdictions. Even though most royalties are attached to the property regardless of owner, nationalizing a mine, for example, could disrupt or even squash royalty agreements, so we're glad the vast majority of assets are located in stable areas.

The mines in South Africa that will come from the buyout of Gold Wheaton don't excite us; the country has problems related to politics, energy, and labor. That said, post acquisition, these assets will represent less than 12% of the company's total net asset value (see our question to Chairman Lassonde below). And unless the mining business completely shuts down there, the royalties will have value.

In total, we would rate the exposure to political risk as low.

Paper/Phinancing

Following the acquisition, FNV will have $200 million in cash and no debt. A $175 million revolving credit line is also available, giving them plenty of firepower for further acquisitions.

The company pays a monthly dividend of 2.5 cents, with a current yield above 1%, higher than Royal Gold. With free cash flow margins in excess of 90%, we fully expect the dividend to increase over the coming years.

The cost of the Gold Wheaton buyout will total C$830 million (60% stock, 40% cash), the new shares equaling an 8% dilution. As stated above, however, revenue will immediately jump 50%, a very good tradeoff.

In the most recent quarterly report, the company's cost of operations was $4 million, against royalty revenue of $49 million, yielding $0.16 per share. This is a financially sound company.

Promotion

The stock is well-known in Canada and is covered by 12 analysts. However, in spite of a larger market cap than Royal Gold, it is mostly off the radar of the much bigger U.S. market. Management says a major U.S. listing is a possibility, but it's our sense this is not coming anytime soon.

That said, the company should grow by leaps and bounds, commanding more attention in the marketplace with each new acquisition and every increase in revenue. And when inflation heats up and investors are looking for a gold stock largely immune to rising costs, the company will promote FNV as a perfect solution.

Price

Like most gold stocks, FNV has undergone a correction, falling as much as 21.2% from its November 2 high of $35.55. We smell an opportunity, as it's now trading at levels not seen since last May. And the company is getting bigger and stronger.

Push

The immediate push is the pending buyout of Gold Wheaton. If approved, revenue will jump substantially, and FNV's portion of income earned from precious metals will exceed that of Royal Gold. The stock is likely to respond positively if the vote goes to the ayes, and receive a re-rating by the market over time.

But this is also where the near-term risk lies. While we think odds are high the acquisition will go through, it must pass two votes: two-thirds of all votes cast, and a majority of GLW shareholders. If it fails one of those tests, the acquisition will be DOA and the stock will likely suffer short-term. Management could consider a higher bid at that point or simply proceed with other acquisitions.

Would we regret buying if that occurred? In a word, no. In the big picture, we still expect growth to be strong without the Gold Wheaton assets, as FNV would then have about $600 million to go shopping with. We certainly hope the deal goes through, but it's the highly experienced management team, the royalty business model, and the growth trajectory of the company we're ultimately putting our money on.

Our Recommendation

If you like the Franco-Nevada story, we suggest placing a bid for one tranche at or below C$29 (our table will reflect the first close below $29). The vote is scheduled for March 8, and if approved, the market will likely react positively. That's not to suggest buying indiscriminately, but the value of the company would clearly be much higher, something the market will recognize sooner or later.

→For U.S. investors, we strongly encourage you NOT to buy the pink sheet version (FNNVF.PK). It trades an average of only 39,000 shares a day, and this low liquidity could hurt you when both buying and selling. If you decide to purchase the stock, we recommend buying the Canadian listing, T.FNV.

[Not set up to buy Canadian stocks? It's easier than you think, and we have a special report devoted to the topic. Check out the recently updated *Casey Research Guide to Investing in Canadian Stocks* here.]

TOP

Pierre Lassonde: Why I Love the Royalty Business

With any new company recommendation, I like to talk with the CEO or chairman. While any executive will paint an optimistic picture of his company, an interview can give us a feel for how the head honcho sees his company, lets us question his goals and projections, and can tell investors what the future might bring. As I think you'll see, Pierre Lassonde not only has the experience and drive to grow his company, he also sees the stars aligning for gold and silver in much the same manner as we do. Read on for some insights into the royalty business, Franco-Nevada, and gold…

Jeff Clark: To start, Pierre, what attracted you to the royalty model?

Pierre Lassonde: Well, we were the very first to come up with that business model back in 1985. We wanted to get into the mining business, but we were a bit like the gentleman farmer – we were gentleman miners and didn't know how to mine. So we were looking for some kind of financial instrument that would allow us to get involved in the industry.

There are three things I love about the royalty business: First, when you buy a royalty, you never have to put up another penny. Your first money is your last money, unlike an operator that has to spend more money on trucks, equipment, etc. You have no exposure to operating or capital expenses, and so I don't care if oil goes to $500 a barrel or employees want 50% higher wages – none of that affects the royalty. The second thing is that a royalty is tied directly to the gold price. Gold goes up 10%, your royalty goes up 10%. The third is that we have the same exploration upside as the operator. If the operator finds more gold on the property or an entirely new deposit, the royalty captures it.

Jeff: On a percentage basis, the explorer would have more upside.

Pierre: Of course. My point is that the operator has to put up all the money, whereas we don't have to put up a cent and still get the upside.

As an example, the very first royalty I bought was on Gold Strike in 1985. I paid $2 million for a 500,000-ounce Resource. Barrick bought the property a year later, started drilling, and ended up finding over 50 million ounces of gold. To date, that royalty has paid out over $600 million, and by the time it's finished, it will have paid out over a billion.

Jeff: Wow. But some royalties only attach to a portion of land.

Pierre: Yes, but all our royalties are essentially on a land package, and thus any deposit found on that land is subject to the royalty. That's why I like to get a lot of acreage in our deals.

Jeff: Is it more difficult to get a royalty on gold than other metals?

Pierre: No, in fact, it's the opposite. When you look at the distribution of primary deposits, there are far more gold deposits in the world than copper or pure silver or any other kind. So, it's easier to build a business based on gold than other metals. Back in the '90s, we actually started a company called Redstone Resources, which centered around base metal royalties, and after seven or eight years we ended up folding it into Franco-Nevada because we just couldn't get enough interest to build the company as big as we wanted.

Jeff: Are most royalties today sold by the operator to finance their work?

Pierre: Yes. Most deals today are from companies that need to raise a lot of money. They can borrow for part of it or do an equity issue, but many times that's not enough.

Jeff: Tell us your big picture with the company, Pierre. What's your goal with FNV? And will gold continue to be a priority?

Pierre: Our priority is and will remain focused on precious metals. We bought the company back from Newmont on January 1, 2008, and at that time it was 50% precious metals and 50% oil and gas. Today, it's about 80% gold and 20% everything else – oil, gas, copper, nickel, etc. And with the Gold Wheaton acquisition, we will be 86% precious metals, about 18% of which will come from platinum group metals.

We have a number of assets in our oil and gas divisions that are world-class assets with great cash flow and very long lives, and we're not going to sell them. And if we see a really good base metal royalty with a 20- or 30-year mine life and low costs, we would definitely pursue it.

Jeff: Any feeling if the Gold Wheaton acquisition will go through?

Pierre: Yes. If you look at the movement in their stock, it's telling you it's essentially a done deal.

Jeff: FNV has sold off.

Pierre: Our stock has not fallen any more than the gold stock indexes, on a percentage basis. I think that once we conclude the deal, the stock is going to have a very strong move upward.

Jeff: What do you base that on?

Pierre: The Gold Wheaton acquisition essentially adds 50% revenue for an 8% dilution. We should hit anywhere from 19 to 24 times cash flow, which would give you a stock price ranging from $43 to $55. Once the street realizes how good a deal this is, I think the stock will rock and roll.

Jeff: Some of GLW's assets are in South Africa; does the risk there concern you?

Pierre: Well, 95% of our royalties are either in North America or Australia. Our portfolio is so conservative that to take a certain amount of risk at this point is not exactly daring. We can definitely afford to increase our risk level.

The two projects we're acquiring in South Africa produce gold and uranium, though our stream is on gold only. Both are operated by First Uranium, which just changed CEOs and got a new mine manager. The tailings retreatment operation, Mine Waste Solutions, is nothing more than technical processing – it's fairly straightforward and not that difficult. The Ezulwini Mine is a little more challenging, no question. It's not a grade A asset, but they're trying hard to straighten out that operation, and from everything that we've seen and the due diligence that has been done, we feel very confident that they will manage to make it go.

Jeff: Would you point to any advantage you have over Royal Gold?

Pierre: Well, they paid us the highest compliment by copying our business model. They loved what we were doing and started doing the same thing. Essentially the company has the same business model but different assets. And so as a potential shareholder you just have to compare the asset mix between the two companies. And you'll find that our assets are more tilted to gold and precious metals. Other than that, they're a well-run company with good people behind it.

Jeff: Other than the GLW acquisition, what else might drive the stock this year?

Pierre: The main reason to own Franco-Nevada is growth. One of the great things about our company is that we've assembled a huge land portfolio. And with the gold price being as high as it is, the operators of these lands have spent huge amounts of money in exploration and have had discoveries, which as I stated increases our royalty payments.

We arranged a 2% royalty on Detour ten years ago, for example, and they now have a 20-million-ounce Resource. And look how much the Kinross-Tasiast property in Mauritania has grown. When you look at just these two operations, it's equivalent to a 4% royalty on Gold Strike, the one I mentioned earlier that's grown 100-fold. That's the kind of scale you're looking at, and that's with just these two deposits.

If you look at our business from the time we took it public three years ago to 2015, we'll have a 23% per year compounded growth rate in our precious metal revenue for seven years in a row. How many other companies have got that? And that's only with the discoveries we know of today. We have a whole bunch of properties that are still being drilled and that over the next 2, 3, 4 years will be announcing further discoveries. So that's the benefit of having a portfolio with two million acres of land and an enormous amount of money being spent on it.

Jeff: Pierre, tell us briefly your outlook for gold and silver.

Pierre: We did a Dow Jones/gold [the Dow index divided by the gold price] chart about ten years ago, and at that point the ratio was about 42:1. We said at the time, wouldn't you rather own an ounce of gold when the ratio is 42:1 than a unit of the Dow? The point is, there are times to own financial assets, like from 1980-2000, and there are times to own hard assets, like from 1967-1980. Well, at the top of the last hard asset bull market, the ratio came back to essentially one. In 1980, the gold price was $800 and the Dow was 800. In 1934, the Dow was 36 and gold was 35. The ratio is down around 8:1 now, but it's not 1:1.

Jeff: You think it's going to 1:1.

Pierre: Well, let me put it this way. Over the last 100 years, it's reached 1:1 twice. Maybe this time it won't, but I wouldn't bet against it. When I look at the $1.5 trillion deficit in the U.S., the debt that's accumulating in Japan and the U.S., and what's going on in Europe, the scenario that is the most likely to happen is not one where governments cut budgets and benefits. They are more likely to take the easy way out, and that unfortunately means printing money, which means a higher gold price.

Look, we may not like the world at $5,000 gold, but are we going to see $5,000 gold? I believe we will.

Jeff: Where do you fall in the inflation/deflation argument?

Pierre: That's a good question. On one hand, there is deflation when you look at U.S. housing prices and unemployment. But when you look at the other side of the coin, you see rising commodity prices – steel, oil, copper – all very inflationary. So where is it all going to end up? Well, there are no politicians in the United States that will stand up for deflation, which means they're going to print. So I think at the end of the day, inflation is going to win.

Jeff: If that's the case, do you subscribe to Doug Casey's view that we'll eventually see a mania in gold and silver?

Pierre: I do, though maybe not for the same reasons as Doug. I think the mania is going to come out of China. I think the Chinese renminbi is going to rise against the dollar, meaning gold in yuan will get cheaper. Then you have inflation perking up in China, their love of gambling, and the deregulation of their gold market. So I believe the mania will mostly come out of China.

Jeff: What about the current correction in gold… does it concern you at all? And would you buy here or wait a little longer?

Pierre: That's a tough question. I'll tell you why. On one hand, I'm well aware of the fact that this is the 10th year in a row the gold price has been higher than the previous year, and nothing grows to the moon. At some point, the record is going to be broken. You also have a lot of people betting the U.S. economy does better this year. And the March to June period is when the gold price is always the weakest.

Against that, I see no sign from the Fed that they're going to raise interest rates in the U.S. I see no sign from the administration that they're going to rein in the deficit – they won't do anything to spoil the party. So when you look at that and at Europe and at what's happening in China, it's very hard to make a case where gold falls substantially. Maybe we'll have a correction to $1,250, which is only about 10%. Could we see a 20% correction? I think there's only a 5% chance of that happening. It's not zero, but I think it's no more than 5%.

Jeff: Just to wrap it, Pierre, what's your advice for gold and silver investors?

Pierre: Well, even though gold has done well, when you look at the amount of money that is not in the gold market, it's hard not to see the potential that still exists. My opinion is that this is a great time to be invested. If you're not in, do get in. This is a great opportunity because precious metals are going to go a lot higher.

How do you do it? You can buy stocks, bullion, or mutual funds, I don't think it matters. You do have to put some work in if you want to buy equities, or else subscribe to a good newsletter such as yours. If you don't want to put in any work, buy a gold ETF. Gold stocks are going to have a better run, but you better know what you're doing.

So yes, this is the time to be invested. The bull market isn't over.

Jeff: Very good, Pierre. Thanks for your time.

→With the growth potential ahead from a stock that's highly leveraged to the gold price, we're ready to add FNV to our portfolio, and think the odds are high we'll be holding it to the end of the bull market.

Jeff Clark, Senior Editor

P.S. You'll notice BIG GOLD arrived a little early this month. We've tuned our publishing schedule to achieve a smoother delivery of all our services, and this letter will now reach your inbox the second Thursday of every month.

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BIG GOLD PORTFOLIO

Security	Symbol (CN)	Rec Date	Rec Price	Close 2/7/11	Market Cap (M)	Change Since Rec	30-Day Change	Current Rec
Metals Funds								
SPDR Gold Trust	GLD	4/20/2007	$68.70	$131.68	$57,120	91.7%	-1.8%	Buy
iShares Silver Trust	SLV	3/18/2008	$19.38	$28.66	$9,340	47.9%	1.3%	Buy
Central Fund of CN	CEF (T.CEF.A)	1/19/2008	$12.83	$19.43	$4,630	51.4%	0.8%	Buy
ETFS Physical Swiss Gold Shares	SGOL	4/15/2010	$115.83	$134.20	$1,070	15.9%	-1.9%	Buy
ETFS Physical Silver Shares	SIVR	5/14/2010	$19.25	$29.20	$386	51.7%	1.2%	Buy
Our metals funds are listed as a Buy, particularly for those who own little to no precious metals. For those looking to add to existing holdings, we'd buy on any significant pullback								
Large Producers								
Barrick	ABX (T.ABX)	3/20/2008	$42.00	$47.83	$47,170	13.9%	-2.5%	Buy 1 tranche at or <$46
Agnico-Eagle	AEM (T. AEM)	10/23/2007	$52.95	$72.04	$12,080	36.1%	0.5%	Buy 1 tranche at or <$68
Kinross	KGC (T.K)	4/20/2007	$14.04	$16.82	$19,030	19.8%	-3.1%	Buy 1 tranche at or <$16
Yamana	AUY (T.YRI)	4/18/2008	$14.49	$11.75	$8,710	-18.9%	-1.2%	Buy1 tranche at or <$11
Mid-Tier Producers								
Randgold	GOLD (LSE:RSS)	12/21/2007	$35.65	$82.05	$7,460	130.2%	-10.1%	HOLD
Eldorado	EGO (T:ELD)	12/15/2009	$11.84	$16.46	$9,020	39.0%	-7.0%	Buy 1 tranche at or <$16
Small Producers								
Alamos Gold	AGIGF (T.AGI)	12/15/2010	$17.25	$16.58	$1,928	-3.9%	-3.9%	Buy 1 tranche at or <C$16
Minefinders	MFN (T.MFL)	7/23/2007	$12.03	$10.57	$698	-12.1%	-0.7%	HOLD
Silvercorp	SVM (T.SVM)	10/15/2009	$4.89	$11.58	$1,910	136.8%	2.6%	Buy 1 tranche at or <$10
Royalties/Streams								
Franco-Nevada	FNNVF (T.FNV)	2/10/2011	TBD	$29.19	$3,342	N/A	N/A	Buy 1 tranche at or <C$29
Royal Gold	RGLD (T.RGL)	$ 39,378.00	$31.67	$47.80	$2,640	$0.51	-5%	Buy 1 tranche at or <$46
Silver Wheaton	SLW (T.SLW)	3/18/2008	$17.62	$34.08	$11,870	93.4%	-0.5%	Buy 1 tranche at or <$30
Gold Stock Funds								
Market Vectors Gold Miners ETF	GDX	8/13/2010	$54.60	$56.12	$7,540	2.8%	-8.5%	Buy
Tocqueville Gold Fund	TGLDX	11/12/2010	$84.55	$84.26	$2,450	-0.3%	-3.7%	Buy
US Global Gold	USERX	5/19/2008	$17.27	$18.06	$296	4.6%	-1.4%	Buy
US Global World Precious Minerals	UNWPX	8/14/2009	$13.71	$21.04	$815	53.5%	0.8%	Buy
Metals funds should be viewed as long-term holdings and for that reason have no Buy Under prices.								

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