



PermRock Royalty Trust (PRT)

Updated September 19th, 2019 by Josh Arnold

Key Metrics

Current Price:	\$7.84	5 Year CAGR Estimate:	12.1%	Volatility Percentile:	0.1%
Fair Value Price:	\$7.20	5 Year Growth Estimate:	4.0%	Momentum Percentile:	7.7%
% Fair Value:	109%	5 Year Valuation Multiple Estimate:	-1.7%	Growth Percentile:	27.8%
Dividend Yield:	12.2%	5 Year Price Target	\$8.76	Valuation Percentile:	51.6%
Dividend Risk Score:	F	Retirement Suitability Score:	C	Total Return Percentile:	86.9%

Overview & Current Events

PermRock Royalty Trust (PRT) is a trust formed in November 2017 by Boaz Energy, a company that is focused on the acquisition, development and operation of oil and natural gas properties in the Permian Basin. It derives 80% of its net profits from the sale of oil and natural gas production from its properties, and distributes dividends every month. In 2018, PermRock produced 1,646 barrels of oil equivalent per day on average, with oil comprising 83% of the output. PermRock trades with a market capitalization of \$95 million. The stock went public in May 2018.

The Permian Basin is the most prolific oil producing area in the U.S. The properties of PermRock consist of long-life reserves in mature, conventional oil fields, with shallow, predictable decline rates. At the end of 2018, the trust's proved reserves stood at 6.4 million barrels, sufficient for about 10 years at the current production rate. However, the trust can pump additional oil via water-flooding techniques, while it will also identify new reserves in the area in the upcoming years. PermRock believes it can produce oil for around 75 more years.

The trust reported Q2 earnings on 8/14/19 and results were comparatively weak against last year's Q2. Oil volumes fell by almost 40% to 134k Bbl, while natural gas volumes declined by a third to 148k Mcf. Total sales volume, in barrel of oil equivalent, or Boe, came to 158k against 255k in the year-ago period. Volumes tend to be volatile given production can move around, but also, the trust's timing of sales can impact one quarter's revenue materially.

In addition, pricing fell for both commodities. Oil was down from \$64 to \$59 per barrel, while natural gas declined from \$2.81 per Mcf to \$2.69. This combination of factors caused revenue and gross profit both to decline significantly year-over-year. Revenue fell by more than half to \$3.1 million from nearly \$8 million in last year's Q2, driving distributable income down from \$7.7 million to \$2.6 million. We're reiterating our estimate of \$0.90 in distributable income this year.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	---	---	---	---	---	---	---	---	---	\$1.28	\$0.90	\$1.09
DPS	---	---	---	---	---	---	---	---	---	\$1.28	\$0.96	\$1.06
Shares¹	---	---	---	---	---	---	---	---	---	12.2	12.2	12.2

PermRock expects to grow its production at a 4.0% annual rate. Thanks to the mature nature of the trust's assets, future production and reserve estimates are highly predictable. Moreover, management believes that it can grow production above this rate via expanded water-flooding operations and drilling of additional wells. Nevertheless, while production growth estimates are reliable, the results of the trust are extremely sensitive to the price of oil and hence it is impossible to predict future earnings with any degree of accuracy. Assuming that PermRock will grow its production by 4% per year on average, and the oil price will remain around its current healthy levels in the upcoming years, we expect the trust to grow its earnings-per-share by approximately 4% per year on average over the next five years.

In 2018, PermRock produced 1,646 barrels of oil equivalent per day on average and posted net profits of \$1.28 per share. Based on the average prices of oil and natural gas in 2018, PermRock estimated that the future net cash flows of

¹ Share count in millions

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its proved reserves are \$346.6 million. With the use of a 10% annual discount factor, the present value of the future net cash flows is \$165.8 million or \$13.6 per share. Of course, this value can move up and down wildly depending upon commodity pricing in the future.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	---	---	---	---	---	---	---	---	---	10.1	8.7	8.0
Avg. Yld.	---	---	---	---	---	---	---	---	---	9.5%	12.2%	12.1%

PermRock is currently trading at a price-to-earnings ratio of 8.7. As the trust has a very short history and it is highly exposed to the price of oil, we prefer to be conservative and assume a fair earnings multiple of 8. PermRock is trading reasonably close to our assumed fair valuation level, so valuation is not likely to impact future returns significantly.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	---	---	---	---	---	---	---	---	---	100%	107%	97%

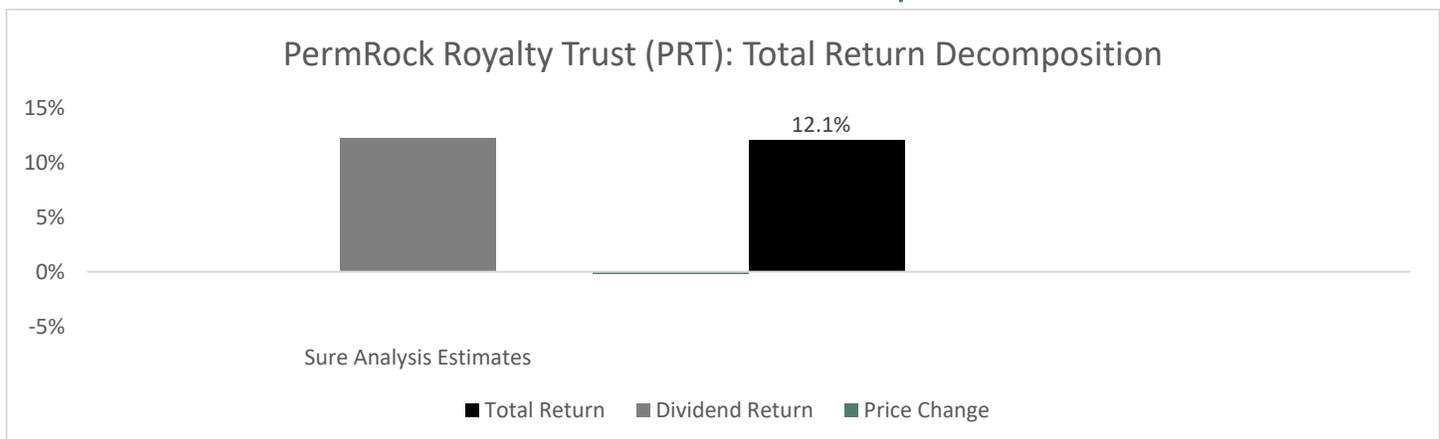
The properties of PermRock are in the Permian Basin, the most prolific oil producing area in the U.S. The trust is suitable for those who want to gain exposure to the booming production in this area. Moreover, Boaz Energy, which manages the trust, has an effective ownership of 58.9% of the net profits of PermRock. This alignment of interests between Boaz Energy and the shareholders of the trust is certainly beneficial for the latter.

On the other hand, PermRock is a pure upstream trust and thus it is far more vulnerable to the gyrations of the price of oil than the well-known oil majors. Moreover, its production is less than 1/2,000th the output of Exxon Mobil, so its scale is extremely small compared to the oil majors. This means that PermRock is much riskier than larger competitors. Whenever the price of oil incurs a strong downtrend, PermRock will suffer. Investors should not allocate a major portion of their portfolio to the trust unless they have strong conviction on high oil prices in the future.

Final Thoughts & Recommendation

PermRock recently enjoyed a major rally thanks to the spike in oil prices. In the absence of a downturn in the oil price, the trust could offer a 12.1% average annual return over the next five years, mostly thanks to its enormous dividend yield. However, as this is a small-scale, pure upstream stock, that is extremely sensitive to the price of oil and will be severely affected in the event of a downturn in the energy sector. We thus rate it as a hold due to the inherent risks.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	18	32	16	18	32	16	18	32	16	18
Gross Profit	5	14		5	14		5	14		5
Gross Margin	27.8%	42.6%		27.8%	42.6%		27.8%	42.6%		27.8%
SG&A Exp.	3	3	1	3	3	1	3	3	1	3
Operating Profit	0	6	16	0	6	16	0	6	16	0
Operating Margin	0.5%	19.5%	96.0%	0.5%	19.5%	96.0%	0.5%	19.5%	96.0%	0.5%
Net Profit	-6	-2	16	-6	-2	16	-6	-2	16	-6
Net Margin	-35.2%	-7.6%	96.0%	-35.2%	-7.6%	96.0%	-35.2%	-7.6%	96.0%	-35.2%
Free Cash Flow	-45	-20		-45	-20		-45	-20		-45

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	119	0	94	119	0	94	119	0	94	119
Cash & Equivalents	1			1			1			1
Accounts Receivable	4	0	0	4	0	0	4	0	0	4
Total Liabilities	53	0	1	53	0	1	53	0	1	53
Accounts Payable	3			3			3			3
Long-Term Debt	36	0	0	36	0	0	36	0	0	36
Shareholder's Equity	66	0	92	66	0	92	66	0	92	66
D/E Ratio	0.54	0.00	0.00	0.54	0.00	0.00	0.54	0.00	0.00	0.54

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets		-4.0%	33.3%		-4.0%	33.3%		-4.0%	33.3%	
Return on Equity		-7.3%	33.8%		-7.3%	33.8%		-7.3%	33.8%	
ROIC		-4.7%	33.8%		-4.7%	33.8%		-4.7%	33.8%	
Shares Out.	12.17	12.17	12.17	12.17	12.17	12.17	12.17	12.17	12.17	12.17
Revenue/Share	1.44	2.61	1.33	1.44	2.61	1.33	1.44	2.61	1.33	1.44
FCF/Share	-3.68	-1.67		-3.68	-1.67		-3.68	-1.67		-3.68

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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