



San Juan Basin Royalty Trust (SJT)

Updated Sept 10th, 2019 by Trond Odegaard

Key Metrics

Current Price:	\$2.40	5 Year CAGR Estimate:	11.7%	Volatility Percentile:	93.0%
Fair Value Price:	\$1.03	5 Year Growth Estimate:	17.5%	Momentum Percentile:	1.0%
% Fair Value:	233%	5 Year Valuation Multiple Estimate:	-15.5%	Growth Percentile:	98.6%
Dividend Yield:	7.2%	5 Year Price Target	\$2.3	Valuation Percentile:	2.1%
Dividend Risk Score:	NA	Retirement Suitability Score:	NA	Total Return Percentile:	17.9%

Overview & Current Events

San Juan Basin Royalty Trust (SJT) is a medium sized gas trust (almost no oil), set up 39 years ago by Southland Royalty Company. The producing properties are all in northern New Mexico, in (not surprisingly) the San Juan Basin. They are currently operated by Hilcorp San Juan, L.P., which acquired the interests in 2017. In 2011, the properties had a remaining expected life of 9 years; we were unable to find a reported current estimated life for the trust (which is probably not a good sign). The trust's assets are static in that no further properties can be added. The trust has no operations, but is merely a pass-through vehicle for the royalties. SJT had royalty income of \$19.4 million in 2018, and has a current market cap of \$107.2 million.

Through May, the trust had declared dividends of \$0.17/share. The trust received no royalties in June, and was informed by Hilcorp that due to an increase in capital expenditures (which are at Hilcorp's sole discretion), there would be no further royalty income in 2019.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
DCFU	\$0.647	\$1.681	\$1.442	\$0.718	\$0.783	\$1.285	\$0.365	\$0.299	\$0.840	\$0.386	\$0.171	\$0.386
DPU	\$0.647	\$1.681	\$1.442	\$0.718	\$0.783	\$1.285	\$0.365	\$0.299	\$0.840	\$0.386	\$0.171	\$0.386
Units¹	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6

Essentially all the royalty income (cash) the trust receives is passed through to unit holders. The trust has generated an average distributable and distributed cash flow of \$0.84/unit annually for the past 10 years. There is no trend, but the volatility inherent in the gas commodity cycle shows plainly. The 4X difference in cash flows from peak to trough years of 2014 to 2016. And now, in 2019, monthly royalty income has ceased for the year starting in June. Presumably they will turn the spigot back on in 2020, and the capex program should result in higher production and higher royalties than would otherwise have been the case. How much higher the production might be, and at what price their gas will sell, is anybody's guess. The trust offers no guidance. We could get out our scratch pad, look at historical production, try to estimate a production boost and a range of natural gas prices over the next five years. But what's the point in perfuming a pig. When the operator can turn off the royalty spigot at his sole discretion, by jacking up the capex program mid-year (original capex announced in March was \$2.65 million; in May it was increased to \$12.6 million), it's all a crapshoot. For the 2024 estimate, keeping this simple, we assume 2018 is a normal year, that SJT will get back to this level of income next year and then maintain it going forward.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
P/DCFU	37.2	12.1	16.1	25.2	19.3	12.1	25.2	18.0	8.9	16.9	14.0	6
Avg. Yld.	2.7%	8.2%	6.2%	4.0%	5.2%	8.3%	4.0%	5.6%	11.3%	5.9%	7.2%	16.7%

¹ Average Weighted Unit count is in millions.

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Their DCFU price multiple has averaged 19.1 over the past 10 years, and given this year's events, it's currently trading considerably below this. However, this average multiple and the current multiple seem high given the risk of royalty trusts in general, and this one specifically. If a growing and well managed midstream oil and gas company has averaged 12 historically, and is worth maybe 8 to 10 going forward, then a royalty trust should not be worth more than 8 going forward, and we think this one is worth closer to 6. After all, royalty trusts have a limited life, they cannot acquire more property – so any growth is entirely organic, and they receive the full shock of the commodity price cycle – there is no buffer between distributable cash flow and dividends, and no ability to hold back on capex to increase the buffer during lean times. And when the music begins to slow down on one of these trusts (i.e., the end of reserves comes into view), or the market gets the slightest hint that the music will slow, the price of a unit will go to zero overnight. And this particular trust has an operator that is not as clearly aligned with trust unit holder interests as one would like.

Safety, Quality, Competitive Advantage, & Recession Resiliency

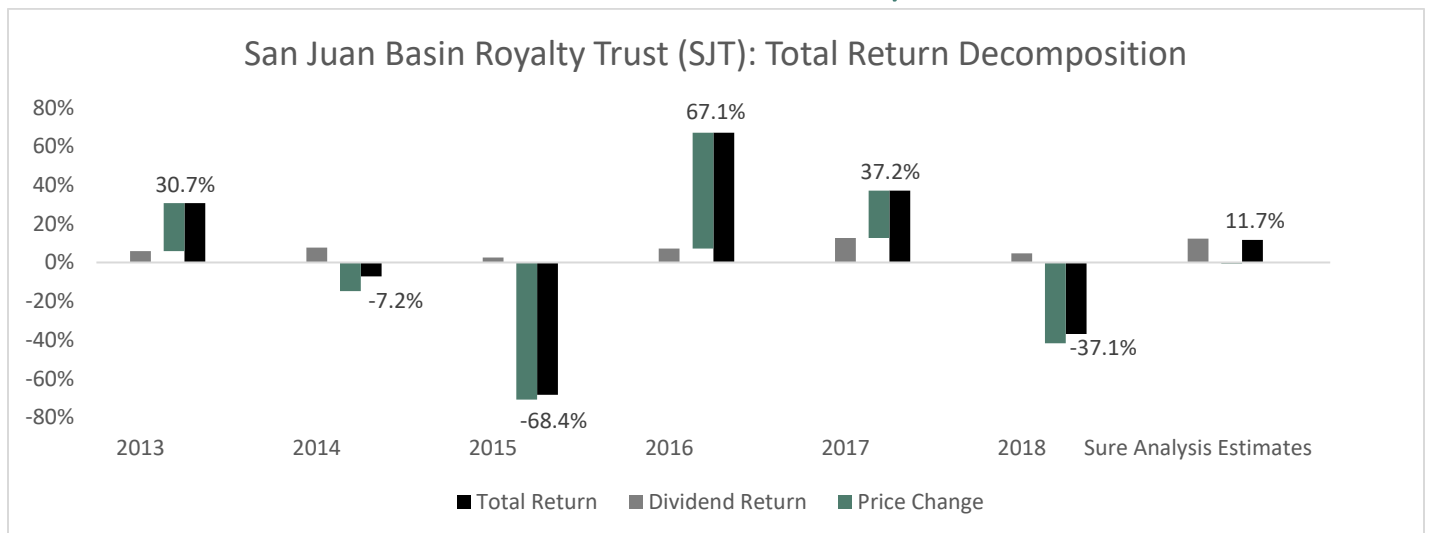
Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

On the positive side, the trust has been in continuous existence for 39 years paying an average 6.1% yield for the last 10 (albeit with considerable volatility in the distributions). Having said this, how much cash this trust distributes annually going forward, and for how long, is anybody's guess. If gas prices maintain at their current level or go up, then the trust may do well (higher distributions, higher unit price) and extend its life – since producers will have an incentive to apply ever-evolving technology to squeeze that extra drop of oil out of the fields. On the other hand, if gas prices head south, so will distributions and the unit price - with alacrity.

Final Thoughts & Recommendation

SJT is a SELL. However, it's trading at the bottom of its long-term price range of \$2.3 to \$47/unit, and the worst of the news on it is probably already baked in. For those who own it, you might want to try to pick your spot to exit, as technicals (MACD) suggest it could get a bounce from here. But fundamentally SJT is not worth anywhere near its current multiple. Investors desiring exposure to the oil and gas industry, or who want a high yield and can stomach some price volatility, can do better with a midstream/upstream business in an MLP or corporate structure.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	32	80	69	35	38	62	20	18	41	19
Gross Profit	32									
Gross Margin	100%									
SG&A Exp.	2									
Operating Profit	30		69	35		62	20	18	41	19
Operating Margin	93.7%		100%	100%		100%	100%	100%	100%	100%
Net Profit	30	78	67	33	36	60	17	14	39	18
Net Margin	93.7%	98.0%	97.8%	95.5%	95.9%	97.2%	87.1%	79.5%	96.1%	92.3%

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	22	20	20	14	16	13	11	12	11	8
Total Liabilities	5	5	20	14	16	13	11	12	11	8
Long-Term Debt	0	0	0	0	0	0	0	0	0	0
Partner's Equity	17	15	13	12	11	9	9	8	7	6
D/E Ratio	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	127%	372%	334%	198%	250%	413%	142%	125%	345%	190%
Return on Equity	173%	496%	482%	265%	316%	589%	188%	169%	545%	289%
ROIC	173%	496%	482%	265%	316%	589%	188%	169%	545%	289%
Shares Out.	46.61	46.61	46.61	46.61	46.61	46.61	46.61	46.61	46.61	46.61
Revenue/Share	0.69	1.72	1.47	0.75	0.82	1.32	0.42	0.38	0.87	0.42

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

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