



# Magellan Midstream Partners (MMP)

Updated February 3<sup>rd</sup>, 2020 by Aristofanis Papadatos

## Key Metrics

<b>Current Price:</b>	\$61	<b>5 Year CAGR Estimate:</b>	12.5%	<b>Market Cap:</b>	\$14.0 B
<b>Fair Value Price:</b>	\$67	<b>5 Year Growth Estimate:</b>	5.0%	<b>Ex-Dividend Date:</b>	2/6/2020
<b>% Fair Value:</b>	91%	<b>5 Year Valuation Multiple Estimate:</b>	2.0%	<b>Dividend Payment Date:</b>	2/14/2020
<b>Dividend Yield:</b>	6.8%	<b>5 Year Price Target</b>	\$86	<b>Years Of Dividend Growth:</b>	19
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	B	<b>Last Dividend Increase:</b>	6.3%

## Overview & Current Events

Magellan Midstream Partners (MMP) has the longest pipeline system of *refined* products, which is linked to nearly half of the total U.S. refining capacity. This segment generates 59% of its total operating income while the transportation and storage of *crude oil* generates 34% of its operating income. MMP has a fee-based model; only ~10% of its operating income depends on commodity prices. That is why it has exhibited impressive resilience in the downturn of the oil market that began in 2014. While most MLPs saw their earnings decline, MMP has grown its earnings-per-share at a 4% average annual rate in the last five years. MMP has a market capitalization of \$14.0 billion.

During the last decade, MMP has invested \$5.4 billion in growth projects and acquisitions and has exhibited much better performance than the vast majority of MLPs. Most MLPs carry excessive amounts of debt, post poor free cash flows due to their capital expenses and dilute their unitholders to a great extent on a regular basis. They also tend to have payout ratios near or above 100%. On the contrary, MMP has posted positive free cash flows for more than 10 consecutive years and has a strong balance sheet. In addition, it does not significantly dilute unitholders and maintains a healthy payout ratio. It is impressive that MMP has increased its unit count by only 1.6% in total in the last nine years. All these attributes confirm the discipline of its management, which invests only in high-return projects.

In late January, MMP reported (1/30/20) financial results for the fourth quarter of fiscal 2019. Adjusted earnings-per-share and distributable cash flow increased 16% and 18%, respectively, primarily thanks to higher shipments of refined products and a higher average transportation rate. It was a record fourth quarter and full year for the earnings and distributable cash flow of MMP. Management provided guidance for 3% distribution growth in 2020 and distribution coverage of 1.25. While this is a strong coverage ratio, we have noted that management tends to be conservative in its guidance to be on the safe side. We thus expect coverage ratio of 1.35, which is still below the 1.40 posted in 2019.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>CF/S</b>	\$1.94	\$2.37	\$2.49	\$3.20	\$4.42	\$4.34	\$4.31	\$4.68	\$4.84	\$5.67	<b>\$5.60</b>	<b>\$7.15</b>
<b>DPS</b>	\$1.46	\$1.56	\$1.78	\$2.10	\$2.51	\$2.92	\$3.25	\$3.52	\$3.80	\$4.04	<b>\$4.16</b>	<b>\$5.31</b>
<b>Units<sup>1</sup></b>	225.0	225.4	226.2	226.7	226.7	227.4	227.8	228.0	229.1	228.7	<b>229.0</b>	<b>232.0</b>

MMP has promising growth prospects, as it has several growth projects under way. The company invested \$1.0 billion in these projects in 2019 and expects to spend \$400 million in 2020. It also has more than \$500 million of potential growth projects under consideration and continues to evaluate their prospects in order to identify the most promising ones.

MMP has grown its cash flow per share at a 5.1% average annual rate in the last five years. In the last four conference calls, management has reiterated its commitment to maintain a distribution coverage ratio of at least 1.20 for the foreseeable future. We continue to expect 5% annual growth in distributable cash flow per share and distribution per share over the next five years.

<sup>1</sup> In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
P/CF	14.6	14.6	17.3	19.8	18.7	15.7	17.6	15.2	13.7	11.0	<b>10.9</b>	<b>12.0</b>
Avg. Yld.	6.0%	5.2%	4.6%	3.9%	3.2%	4.0%	4.7%	4.9%	5.7%	6.4%	<b>6.8%</b>	<b>6.2%</b>

MMP is trading at a price-to-cash flow ratio of 10.9, which is lower than its 10-year average ratio of 15.8. In order to be conservative, we assume a fair price-to-cash flow ratio of 12.0 for this MLP. If the stock approaches our fair valuation level over the next five years, it will enjoy a 2.0% annualized boost to total returns.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	75.3%	65.8%	71.5%	65.6%	56.8%	67.3%	75.4%	75.2%	78.5%	71.2%	<b>74.3%</b>	<b>74.3%</b>

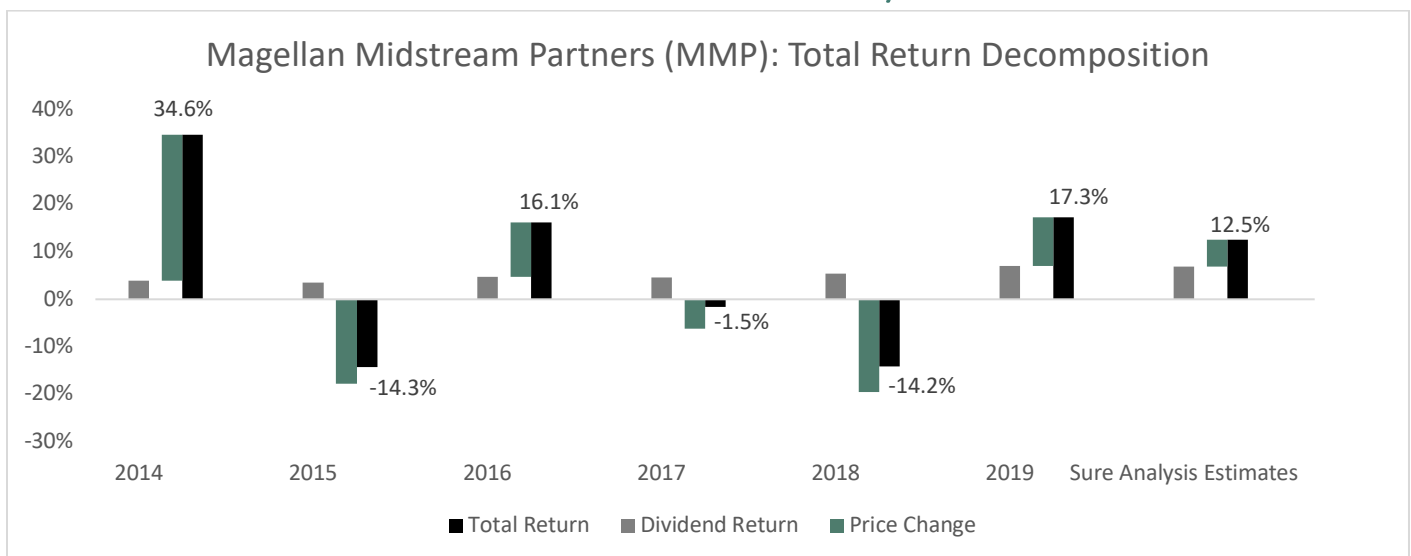
The competitive advantage of MMP comes from its fee-based model, its great scale and its discipline to invest only in high-return projects. MMP has grown its dividend for 70 consecutive quarters and has raised its annual dividend at a 12% average annual rate since 2001. In the last four conference calls, management has remained confident that the MLP will maintain a distribution coverage ratio of at least 1.2 in the years ahead. All these facts are testaments to the strength of its business model and its great discipline to invest only in high-return projects. Moreover, management has stated that it does not expect to issue any equity to fund current growth projects. Thanks to its fee-based model, MMP proved resilient during the downturn of the oil market that began in 2014.

On the other hand, investors should not jump to the conclusion that MMP is immune to recessions. In the Great Recession, its earnings-per-share fell -32%, from \$1.64 in 2008 to \$1.11 in 2009. As a recession has not occurred for a whole decade, investors should keep this risk factor in mind.

## Final Thoughts & Recommendation

MMP is one of the safest and highest-quality MLPs around. It has raised its dividend for 70 consecutive quarters and has ample room to continue to raise it for years thanks to its promising pipeline of growth projects, healthy payout ratio and strong balance sheet. The stock is offering a reliable 6.8% dividend yield, which is very attractive amid low interest rates. MMP could offer a 12.5% average annual return over the next five years and thus it maintains its buy rating.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Revenue</b>	1557	1749	1772	1948	2360	2188	2205	2508	2827	2728
<b>Gross Profit</b>	780	921	987	1,227	1,604	1,574	1,534	1,675	1,857	1,862
<b>Gross Margin</b>	50.1%	52.7%	55.7%	63.0%	68.0%	71.9%	69.6%	66.8%	65.7%	68.3%
<b>SG&amp;A Exp.</b>	95	99	109	132	148	150	147	166	194	197
<b>D&amp;A Exp.</b>	109	121	128	142	162	167	178	197	265	
<b>Operating Profit</b>	403	516	549	699	955	901	858	932	1013	1,035
<b>Operating Margin</b>	25.9%	29.5%	31.0%	35.9%	40.5%	41.2%	38.9%	37.2%	35.9%	37.9%
<b>Net Profit</b>	312	414	436	582	840	819	803	870	1334	1,021
<b>Net Margin</b>	20.0%	23.7%	24.6%	29.9%	35.6%	37.4%	36.4%	34.7%	47.2%	37.4%
<b>Free Cash Flow</b>	203	378	292	352	744	449	299	573	801	
<b>Income Tax</b>	1	2	3	5	5	2	3	4	0	1

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Total Assets</b>	3718	4045	4420	4821	5501	6042	6772	7394	7748	
<b>Cash &amp; Equivalents</b>	7	210	328	25	17	29	15	161	218	
<b>Accounts Receivable</b>	92	82	91	116	84	84	106	139	104	
<b>Inventories</b>	216	259	222	187	158	131	134	182	186	
<b>Goodwill &amp; Int. Ass.</b>	57	68	67	61	58	55	105	106	104	
<b>Total Liabilities</b>	2248	2582	2904	3173	3633	4020	4680	5265	5104	
<b>Accounts Payable</b>	41	66	112	76	97	104	77	105	139	
<b>Long-Term Debt</b>	1906	2152	2393	2685	2967	3440	4087	4524	4271	
<b>Shareholder's Equity</b>	1455	1463	1516	1647	1868	2022	2092	2130	2643	

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Return on Assets</b>	9.1%	10.7%	10.3%	12.6%	16.3%	14.2%	12.5%	12.3%	17.6%	
<b>Return on Equity</b>	23.5%	28.3%	29.2%	36.8%	47.8%	42.1%	39.0%	41.2%	55.9%	
<b>Units Out.</b>	225.0	225.4	226.2	226.7	226.7	227.4	227.8	228.0	229.1	228.7
<b>Revenue/Share</b>	7.11	7.74	7.82	8.58	10.37	9.60	9.67	10.98	12.37	11.92
<b>FCF/Share</b>	0.93	1.67	1.29	1.55	3.27	1.97	1.31	2.51	3.50	

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

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