



Magellan Midstream Partners (MMP)

Updated May 5th, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	\$44	5 Year CAGR Estimate:	16.8%	Market Cap:	\$9.9 B
Fair Value Price:	\$56	5 Year Growth Estimate:	5.0%	Ex-Dividend Date:	5/7/2020
% Fair Value:	78%	5 Year Valuation Multiple Estimate:	5.1%	Dividend Payment Date:	5/15/2020
Dividend Yield:	9.3%	5 Year Price Target	\$72	Years Of Dividend Growth:	20
Dividend Risk Score:	C	Retirement Suitability Score:	B	Last Dividend Increase:	1.7%

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 exhibited impressive resilience in the downturn of the oil market between 2014 and 2017. 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 \$9.9 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 early May, MMP reported (5/1/20) financial results for the first quarter of fiscal 2020. Distributable cash flow fell -4%, from \$318 million to \$306.5 million, primarily due to lower transportation and terminal revenue in the crude oil segment. While MMP has a resilient business model, it is not immune to the collapse in the demand for refined products caused by the pandemic. As a result, it lowered its guidance for distributable cash flow this year from \$1.2 billion to \$1.0-\$1.075 billion while it froze its distribution for the first time in 71 quarters. MMP intends to maintain its quarterly distribution constant for the rest of the year and expects a distribution coverage ratio of 1.10-1.15. Due to the effect of the pandemic on MMP, we have lowered our forecast for distributable cash flow per unit from \$5.60 to \$4.70.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
CF/S	\$1.94	\$2.37	\$2.49	\$3.20	\$4.42	\$4.34	\$4.31	\$4.68	\$4.84	\$5.67	\$4.70	\$6.00
DPS	\$1.46	\$1.56	\$1.78	\$2.10	\$2.51	\$2.92	\$3.25	\$3.52	\$3.80	\$4.04	\$4.11	\$5.25
Units¹	225.0	225.4	226.2	226.7	226.7	227.4	227.8	228.0	229.1	228.7	229.0	232.0

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, despite the pandemic. 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. We view the pandemic as a temporary headwind and expect the energy market to recover from next year. MMP has grown its cash flow per share at a 5.1% average annual rate in the last five years. In the last five conference calls, management has reiterated its commitment to maintain a distribution coverage ratio of at least 1.20 in the long run. We continue to expect 5% annual growth in distributable cash flow per share and distribution per unit over the next five years.

¹ 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	9.4	12.0
Avg. Yld.	6.0%	5.2%	4.6%	3.9%	3.2%	4.0%	4.7%	4.9%	5.7%	6.4%	9.3%	7.3%

MMP is trading at a price-to-cash flow ratio of 9.4, which is much 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 5.1% 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%	87.4%	87.4%

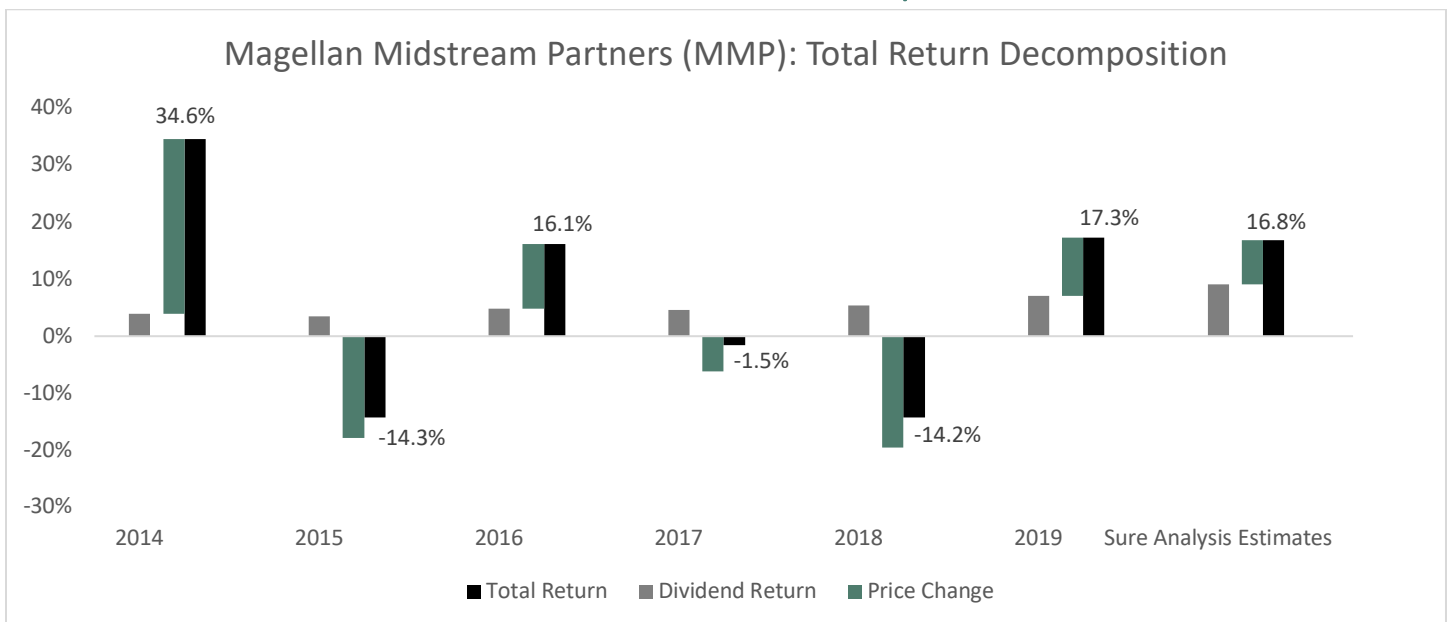
The competitive advantage of MMP comes from its fee-based model, its great scale and its discipline to invest only in high-return projects. MMP grew its dividend for 70 consecutive quarters before the recent freeze and has raised its annual dividend at a 12% average annual rate since 2001. This record is a testament to the strength of the business model and the great discipline of management 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. In the ongoing recession, earnings will dip again but MMP should endure the downturn and enjoy a strong recovery as soon as the pandemic subsides.

Final Thoughts & Recommendation

MMP is one of the safest and highest-quality MLPs around. Its -32% correction amid the pandemic has presented an exceptional opportunity to invest in this best-of-breed MLP. MMP could offer a 16.8% average annual return over the next five years, partly thanks to its 9.3% distribution yield, and thus it earns a 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
Revenue	1,557	1,749	1,772	1,948	2,360	2,188	2,205	2,508	2,827	2,728
Gross Profit	780	921	987	1,227	1,604	1,574	1,534	1,675	1,857	1,862
Gross Margin	50.1%	52.7%	55.7%	63.0%	68.0%	71.9%	69.6%	66.8%	65.7%	68.3%
SG&A Exp.	95	99	109	132	148	150	147	166	194	197
D&A Exp.	109	121	128	142	162	167	178	197	265	246
Operating Profit	403	516	549	699	955	901	858	932	1,013	1,035
Operating Margin	25.9%	29.5%	31.0%	35.9%	40.5%	41.2%	38.9%	37.2%	35.9%	37.9%
Net Profit	312	414	436	582	840	819	803	870	1,334	1,021
Net Margin	20.0%	23.7%	24.6%	29.9%	35.6%	37.4%	36.4%	34.7%	47.2%	37.4%
Free Cash Flow	203	378	292	352	744	449	299	573	801	377
Income Tax	1	2	3	5	5	2	3	4	0	1

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	3,718	4,045	4,420	4,821	5,501	6,042	6,772	7,394	7,748	8,438
Cash & Equivalents	7	210	328	25	17	29	15	161	218	58
Accounts Receivable	92	82	91	116	84	84	106	139	104	125
Inventories	216	259	222	187	158	131	134	182	186	184
Goodwill & Int. Ass.	57	68	67	61	58	55	105	106	104	101
Total Liabilities	2,248	2,582	2,904	3,173	3,633	4,020	4,680	5,265	5,104	5,723
Accounts Payable	41	66	112	76	97	104	77	105	139	151
Long-Term Debt	1,906	2,152	2,393	2,685	2,967	3,440	4,087	4,524	4,271	4,706
Shareholder's Equity	1,455	1,463	1,516	1,647	1,868	2,022	2,092	2,130	2,643	2,715

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	9.1%	10.7%	10.3%	12.6%	16.3%	14.2%	12.5%	12.3%	17.6%	12.6%
Return on Equity	23.5%	28.3%	29.2%	36.8%	47.8%	42.1%	39.0%	41.2%	55.9%	38.1%
Units Out.	225.0	225.4	226.2	226.7	226.7	227.4	227.8	228.0	229.1	228.7
Revenue/Share	7.11	7.74	7.82	8.58	10.37	9.60	9.67	10.98	12.37	11.92
FCF/Share	0.93	1.67	1.29	1.55	3.27	1.97	1.31	2.51	3.50	1.65

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

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