



Cross Timbers Royalty Trust (CRT)

Updated November 18th, 2020 by Aristofanis Papadatos

Key Metrics

Current Price:	\$7.90	5 Year CAGR Estimate:	6.5%	Market Cap:	\$47 M
Fair Value Price:	\$5.20	5 Year Growth Estimate:	4.0%	Ex-Dividend Date¹:	11/30/20
% Fair Value:	153%	5 Year Valuation Multiple Estimate:	-8.1%	Dividend Payment Date:	12/15/20
Dividend Yield:	9.4%	5 Year Price Target	\$6.30	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Last Dividend Increase:	N/A

Overview & Current Events

Cross Timbers Royalty Trust (CRT) is a medium sized oil and gas trust (about 50/50), set up in 1991 by XTO Energy. It is a combination trust: unit holders have a 90% net profit interest in *producing properties* in Texas, Oklahoma, and New Mexico; and a 75% net profit interest in *working interest properties* in Texas and Oklahoma. A working interest property is one where the unit holder shares in production expense and development cost. This means that should development costs exceed profits no further profits will be paid from these properties until excess costs have been recovered.

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. CRT had royalty income of \$9.1 million in 2018 and \$5.9 million in 2019.

In early November, CRT reported (11/6/20) financial results for the third quarter of fiscal 2020. Due to the pandemic, its average realized prices of oil and gas plunged -47% and -24%, respectively, over last year's quarter. Production of oil and gas grew 16% and 7%, respectively, and thus somewhat offset the effect of suppressed commodity prices. Overall, net income slumped -35%. The trust does not provide any guidance for the running year.

In the first eleven months of this year, CRT offered markedly generous dividends, as it distributed total dividends of \$0.67. We expect a dividend of \$0.07 per share in December and thus we expect an annual dividend of \$0.74, which corresponds to a dividend yield of 9.4% at the current stock price. Nevertheless, investors should keep in mind that CRT is highly vulnerable to the pandemic, particularly if the downturn lasts longer than currently anticipated.

Growth on a Per-Unit Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
DCFU	\$2.788	\$2.993	\$2.482	\$2.315	\$2.658	\$1.355	\$1.061	\$1.009	\$1.426	\$0.87	\$0.74	\$0.90
DPU	\$2.788	\$2.993	\$2.482	\$2.315	\$2.658	\$1.355	\$1.061	\$1.009	\$1.426	\$0.87	\$0.74	\$0.90
Units²	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0

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 \$2.00/unit annually for the past 10 years, though with a noticeable decrease in the past five years (especially last year). The distribution trend essentially parallels the trend in natural gas prices. Moreover, CRT estimates that the rate of natural production decline of its oil and gas properties is 6%-8% per year. This is a significant headwind for future returns. Given the low comparison base formed this year due to the coronavirus, we expect CRT to grow its distributable cash flow by 4.0% per year on average over the next five years.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
P/DCFU	13.2	14.8	15.3	12.2	8.8	11.2	14.6	16.2	9.0	12.3	10.7	7.0
Avg. Yld.	7.6%	6.7%	6.5%	8.2%	11.4%	8.9%	6.8%	6.2%	11.1%	8.1%	9.4%	14.3%

¹ Estimated date.

² Average Weighted Unit count is in millions.

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The trust's DCFU price multiple has averaged 12.8 over the past 10 years. CRT is now trading at a lower valuation multiple of 10.7 but we assume a fair valuation multiple of 7.0 for the trust due to its declining production volume. If CRT trades at our assumed fair valuation level in five years, it will incur an -8.1% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

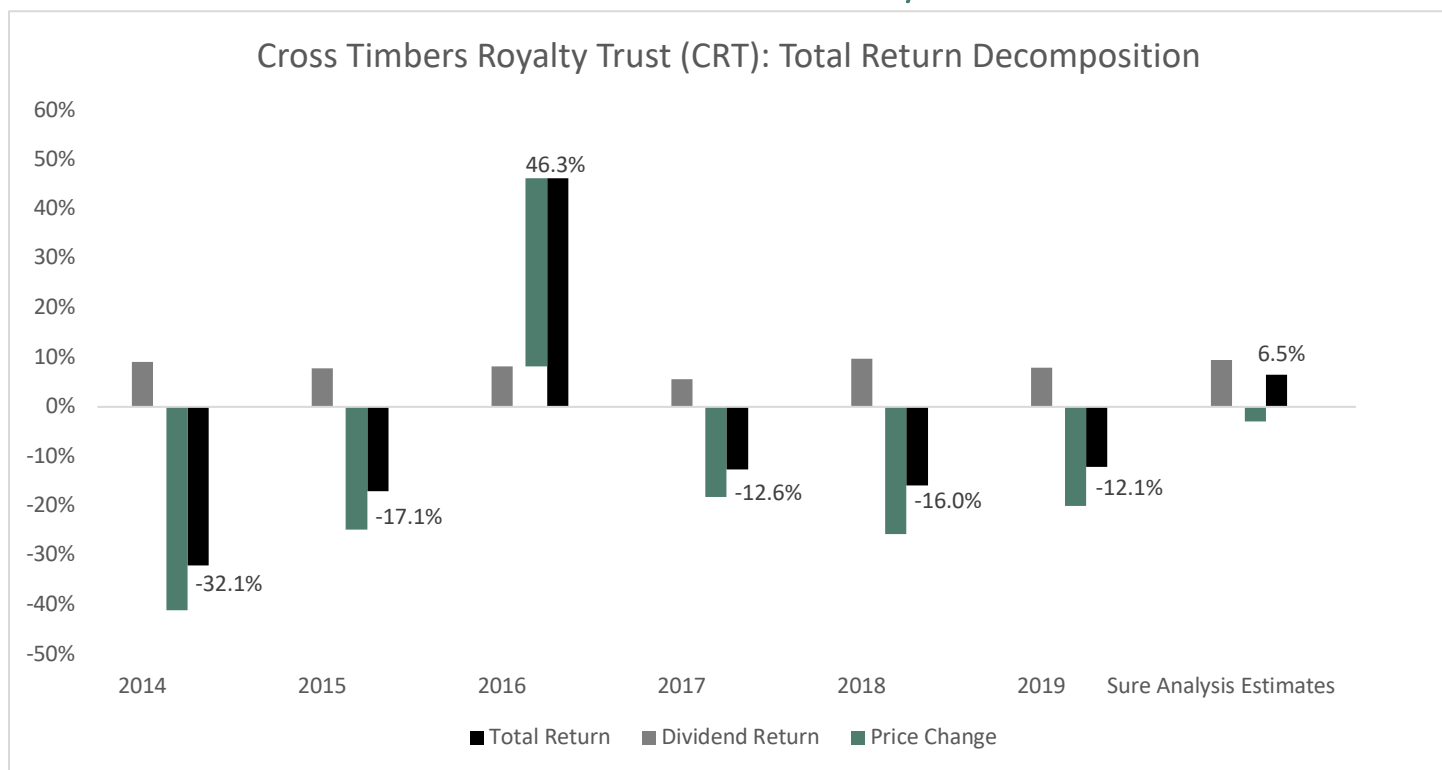
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

On the positive side, the trust has been in continuous existence for 29 years paying an average 8.0% yield in the last decade (albeit with some volatility in the distributions). However, future distributions are highly unpredictable due to the absence of any guidance and the unknown path of oil and gas prices. If oil and gas prices recover towards last year's levels, the trust will continue paying a nice dividend and the unit price may recover – unless investors sense that reserves are beginning to dry up. If oil and gas prices increase, then the trust should do well (higher distributions, higher unit price) and will be able to extend its life – since the producer will have an incentive to apply ever-evolving technology to squeeze that extra volume out of the fields. On the other hand, if the downturn from the pandemic lasts longer than currently anticipated, the trust is likely to exhibit poor performance.

Final Thoughts & Recommendation

CRT slumped -50% early this year due to the spread of the coronavirus and the resultant collapse of the oil price. We expect the pandemic to attenuate at the second half of next year and thus we expect CRT to recover. However, the stock has rallied 25% since our last research report, in August, and thus it has become less attractive. We expect CRT to offer a 6.5% average annual return over the next five years, primarily thanks to its 9.4% dividend yield. We thus rate the stock as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	17	18	15	14	16	9	8	7	9	6
Gross Margin	0	0	0	0	1	0	0	1	1	1
SG&A Exp.	2	---	---	---	1	0	1	1	---	---
D&A Exp.	17	18	15	14	16	8	6	6	9	5
Operating Profit	97.6%	97.7%	97.4%	97.2%	96.9%	91.5%	84.1%	91.3%	93.5%	88.2%
Operating Margin	17	18	15	14	16	8	6	6	9	5
Net Profit	97.6%	97.7%	97.4%	97.2%	96.9%	91.5%	84.4%	91.4%	93.7%	88.6%
Net Margin	15	---	---	---	15	8	6	5	---	---
Distr. Cash Flow	17	18	15	14	16	9	8	7	9	---

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	16	15	14	13	12	12	11	11	10	10
Total Liabilities	1	1	1	1	1	1	2	1	2	2
Partner's Equity	15	13	13	12	11	11	10	9	9	8

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	100.8%	118%	105%	104%	127%	68.4%	55.4%	54.5%	81.9%	53.1%
Return on Equity	108.9%	129%	115%	114%	140%	75.5%	62.3%	63.0%	96.0%	63.0%
ROIC	108.9%	129%	115%	114%	140%	75.5%	62.3%	63.0%	96.0%	63.0%
Shares Out.	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Revenue/Share	2.86	3.06	2.55	2.38	2.74	1.48	1.26	1.10	1.52	0.99
DCF/Share	2.51	---	---	---	2.52	1.28	0.95	0.91	---	---

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

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