



San Juan Basin Royalty Trust (SJT)

Updated November 19th, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	\$7.50	5 Year CAGR Estimate:	0.8%	Market Cap:	\$349 M
Fair Value Price:	\$4.80	5 Year Growth Estimate:	0.0%	Ex-Dividend Date¹:	11/26/21
% Fair Value:	156%	5 Year Valuation Multiple Estimate:	-8.5%	Div. Payment Date:	12/13/21
Dividend Yield:	8.0%	5 Year Price Target	\$4.80	Years Of Dividend Growth:	1
Dividend Risk Score:	F	Retirement Suitability Score:	C	Last Dividend Increase:	N/A

Overview & Current Events

San Juan Basin Royalty Trust (SJT) is a medium sized gas trust (it produces a negligible amount of oil), set up 39 years ago by Southland Royalty Company. The producing properties are all in northern New Mexico, in the San Juan Basin. They are currently operated by Hilcorp San Juan, L.P., which acquired the interests in 2017. 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 \$8.8 million in 2020, and has a current market capitalization of \$349 million.

In 2011, SJT 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). Moreover, due to the volatility of the price of natural gas, the trust revises its estimated reserves pronouncedly every year, as lower prices mean that some reserves are not economical to produce. As a result, it is essentially impossible to calculate the lifetime of reserves with any degree of precision.

In mid-November, SJT reported (11/15/2021) financial results for the third quarter of fiscal 2021. Thanks to the impressive rally of the price of natural gas, which has resulted from pent-up demand after the pandemic and tight supply, distributable income per unit grew from \$0.00 to \$0.12. Nevertheless, given the rally of the gas price to a 7-year high, we expected higher distributions. Based on distributions per unit of \$0.50 in the first 10 months of the year, we have lowered our forecast for annual distributable income per unit from \$0.68 to \$0.60.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
DCFU	\$1.442	\$0.718	\$0.783	\$1.285	\$0.365	\$0.299	\$0.840	\$0.386	\$0.174	\$0.159	\$0.60	\$0.60
DPU	\$1.442	\$0.718	\$0.783	\$1.285	\$0.365	\$0.299	\$0.840	\$0.386	\$0.174	\$0.159	\$0.60	\$0.60
Units²	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 annual distributable and distributed cash flow of \$0.65 per unit for the past 10 years. However, distributions have been extremely volatile due to the dramatic swings of the price of natural gas. That's why the trust offers no guidance. This year, the price of natural gas has rallied to a 7-year high thanks to pent-up demand after the pandemic and tight supply. As this year will form a high comparison base and given the natural decline of production of SJT in the long run, we expect distributable income per unit to be approximate flat in 2026. Investors should not expect the current sky-high prices of natural gas to remain in place for years, as supply should catch up with demand at some point, most likely in 2022.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
P/DCFU	16.1	25.2	19.3	12.1	25.2	18.0	8.9	16.9	21.2	16.6	12.5	8.0
Avg. Yld.	6.2%	4.0%	5.2%	8.3%	4.0%	5.6%	11.3%	5.9%	4.7%	6.0%	8.0%	12.5%

¹ Estimated date.

² Average Weighted Unit count is in millions.

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SJT has traded at an average price-to-DCFU of 18.0 over the last decade. The trust is currently trading at a price-to-DCFU ratio of 12.5. Due to the natural decline of the production of SJT in the long run and the uncertainty over the lifetime of its reserves, we assume a fair price-to-DCFU of 8.0 for this trust. If SJT trades at this valuation level in five years, it will incur an -8.5% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

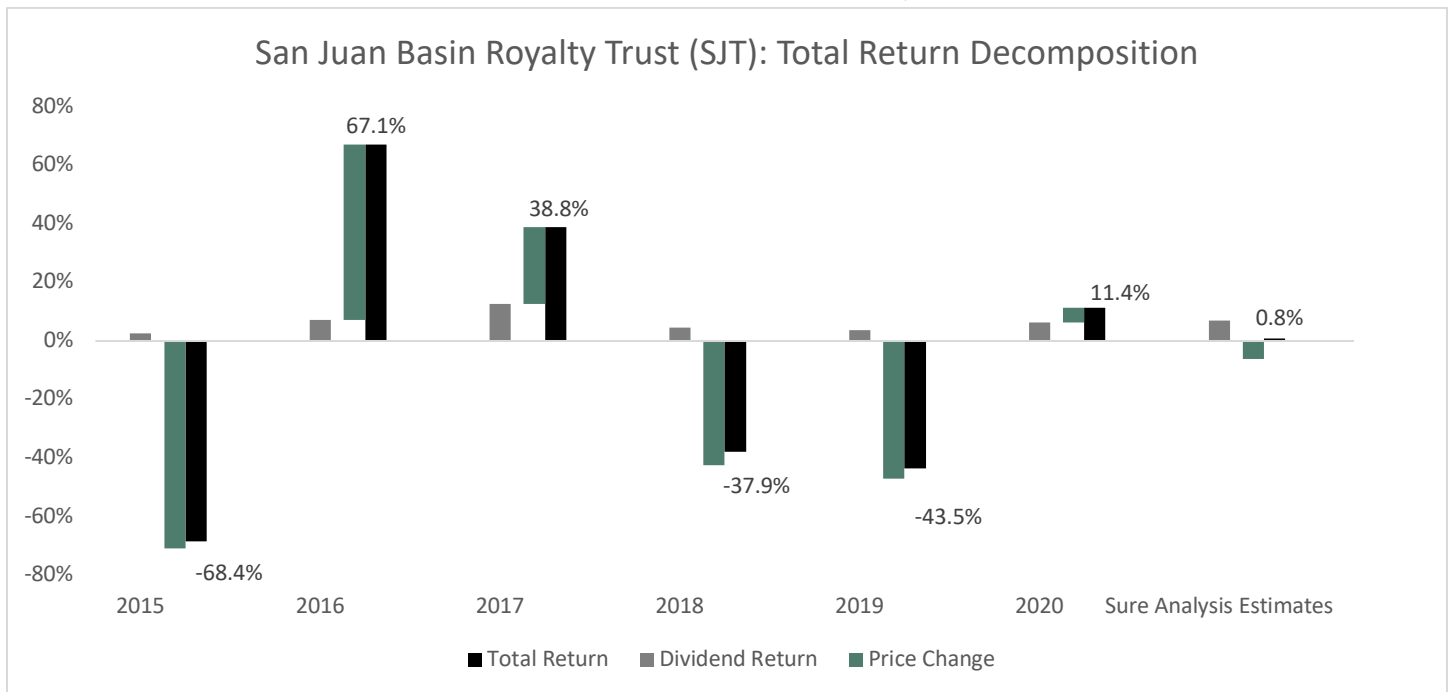
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

SJT has been in continuous existence for 39 years and has offered an average 6.1% yield for the last 10 years (albeit with considerable volatility in the distributions). Having said that, it is impossible to forecast future distributions beyond this year due to the dramatic swings of gas prices. SJT has proved highly vulnerable to the downturns of the energy market, as evidenced in 2015-2016 and 2020. It suspended its distribution for six months in 2019 and four months in 2020 due to low natural gas prices. At high gas prices, the trust can extend its life, as it will have an incentive to apply ever-evolving technology to squeeze extra amounts of gas out of the fields. On the other hand, when the music begins to slow down on 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 can plummet overnight. And this particular trust has an operator that is not as clearly aligned with trust unit holder interests as one would like.

Final Thoughts & Recommendation

SJT is recovering strongly from the pandemic this year thanks to the rally of natural gas prices to a 7-year high. However, due to its rich valuation, the trust could offer a poor average total return over the next five years. As a result, SJT receives a sell rating. Even at more opportune stock prices, SJT is suitable only for the investors who can stomach the extreme volatility of natural gas prices and the resultant volatility of the stock price.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	69	35	38	62	20	18	41	19	10	9
SG&A Exp.	---	---	---	---	---	---	---	1	2	1
Operating Profit	69	35		62	20	18	41	18	8	7
Net Profit	67	33	36	60	17	14	39	18	8	7
Net Margin	97.8%	95.5%	95.9%	97.2%	87.1%	79.5%	96.1%	92.5%	81.7%	83.9%

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	20	14	16	13	11	12	11	8	7	6
Total Liabilities	7	1	5	4	2	4	4	2	1	1
Long-Term Debt	---	---	---	---	---	---	---	---	---	---
Partner's Equity	13	12	11	9	9	8	7	6	5	5

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	334%	198%	250%	413%	142%	125%	345%	190%	112%	115%
Return on Equity	482%	265%	316%	589%	188%	169%	545%	289%	143%	140%
ROIC	482%	265%	316%	589%	188%	169%	545%	289%	143%	140%
Shares Out.	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6
Revenue/Share	1.47	0.75	0.82	1.32	0.42	0.38	0.87	0.42	0.21	0.19

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

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