



Cross Timbers Royalty Trust (CRT)

Updated May 30th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	\$19	5 Year CAGR Estimate:	-3.1%	Market Cap:	\$114 M
Fair Value Price:	\$13	5 Year Growth Estimate:	-5.0%	Ex-Dividend Date:	5/27/22
% Fair Value:	147%	5 Year Valuation Multiple Estimate:	-7.4%	Dividend Payment Date:	6/14/22
Dividend Yield:	7.6%	5 Year Price Target	\$10	Years Of Dividend Growth:	1
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Sell

Overview & Current Events

Cross Timbers Royalty Trust (CRT) is an 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 \$5.3 million in 2020 and \$7.4 million in 2021.

In mid-May, CRT reported (5/13/22) financial results for the first quarter of fiscal 2022. Production of gas plunged -43% due to timing of sales but production of oil more than tripled for the same reason. Moreover, the average realized prices of oil and gas grew 37% and 78%, respectively, thanks to the sanctions of western countries on Russia, which have sent the benchmark prices of oil and gas to 13-year highs. As a result, distributable cash flow (DCF) per unit grew 65%, from \$0.17 to \$0.28. The trust does not provide any guidance for the running year.

We do not expect the aforementioned sanctions to be withdrawn in the short run and hence CRT will probably post 7-year high DCF this year. Based on its distributions in the first five months of the year, CRT is offering an annualized yield of 7.6%. However, we expect the oil price to deflate whenever the ongoing war in Ukraine ends. In addition, the huge natural decline of the fields and the high operating costs of CRT experienced in 2021 raise a big red flag for this trust.

Growth on a Per-Unit Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
DCFU	\$2.482	\$2.315	\$2.658	\$1.355	\$1.061	\$1.009	\$1.426	\$0.87	\$0.77	\$1.10	\$1.44	\$1.11
DPU	\$2.482	\$2.315	\$2.658	\$1.355	\$1.061	\$1.009	\$1.426	\$0.87	\$0.77	\$1.10	\$1.44	\$1.11
Units¹	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 \$1.50/unit annually for the past 10 years, though with a noticeable decrease in the past seven years (especially in the last three years). The distribution trend essentially parallels the trend in oil and 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 high comparison base formed this year thanks to favorable oil and gas prices, we expect a -5% average annual decline of distributable cash flow until 2027.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
P/DCFU	15.3	12.2	8.8	11.2	14.6	16.2	9.0	12.3	9.0	10.0	13.2	9.0
Avg. Yld.	6.5%	8.2%	11.4%	8.9%	6.8%	6.2%	11.1%	8.1%	11.1%	10.0%	7.6%	11.1%

¹ Average Weighted Unit count is in millions.

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The trust's DCFU price multiple has averaged 11.9 over the past 10 years. CRT is now trading at a valuation multiple of 13.2 but we assume a fair valuation multiple of 9.0 for the trust due to its declining production volume. If CRT trades at our assumed fair valuation level in five years, it will incur a -7.4% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

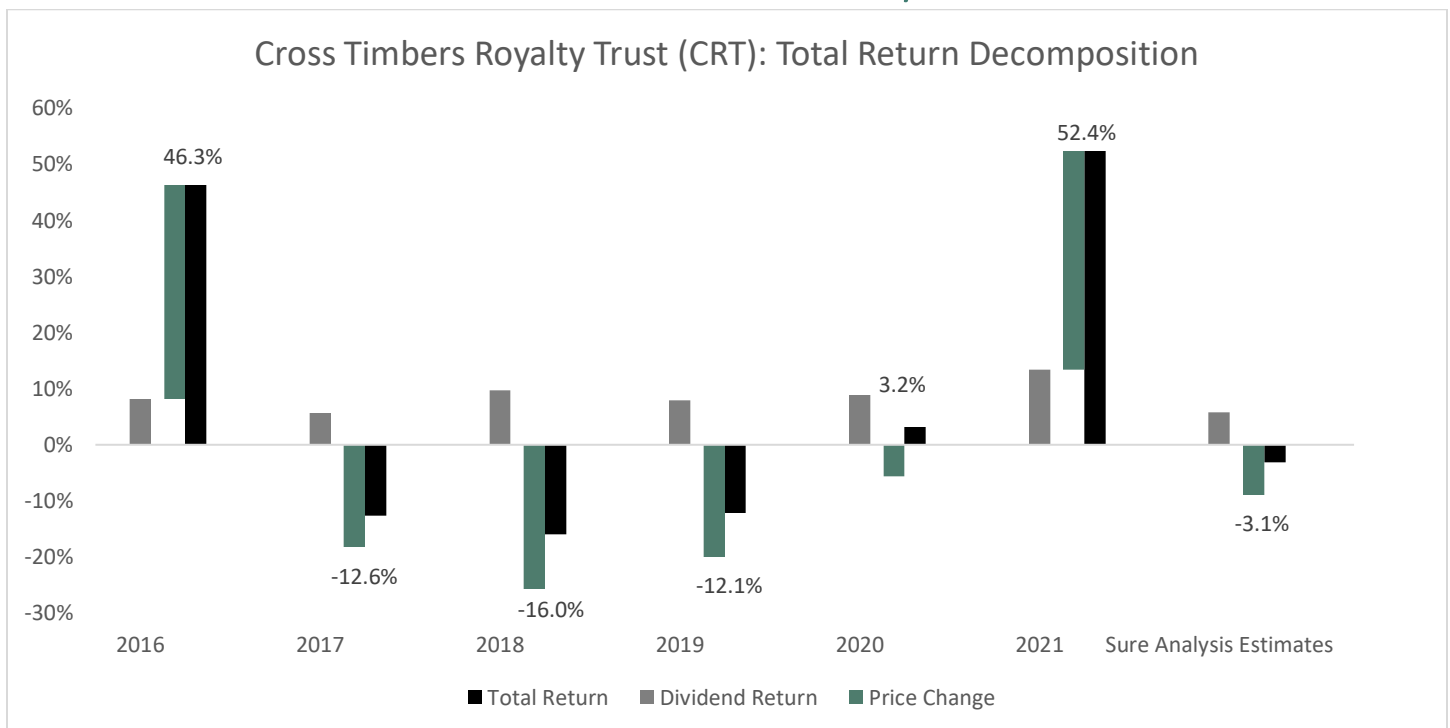
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

On the positive side, the trust has been in continuous existence for 31 years paying an average 8.8% 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 remain around current levels or increase, the trust will continue offering a nice yield. In such a case, the trust should do well and will be able to extend its life – since the producer will have an incentive to apply ever-evolving technology to squeeze extra volume out of the fields. On the other hand, if oil and gas prices go through a major downturn, the trust is likely to exhibit poor performance.

Final Thoughts & Recommendation

CRT slumped -50% in early 2020 due to the spread of the coronavirus and the resultant collapse of the oil price. However, the pandemic has subsided and the prices of oil and gas have rallied to 13-year highs, mostly thanks to the war between Russia and Ukraine. Nevertheless, we expect the oil price to deflate after the end of the ongoing war and CRT to offer a poor average annual return over the next five years. The 7.6% distribution is certainly attractive, but investors should be aware of the high cyclical nature of oil and gas prices and the long-term decline of the production of CRT. Given also the steep decline in its production in 2021 and its inability to take full advantage of exceptionally high prices of oil and gas due to high operating costs, CRT receives a sell rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	15	14	16	9	8	7	9	6	5	7
SG&A Exp.	---	---	1	0	0	1	1	1	1	1
D&A Exp.	15	14	16	8	6	6	9	5	5	7
Operating Profit	97.4%	97.2%	96.9%	91.5%	84.1%	91.3%	93.5%	88.2%	88.0%	89.7%
Operating Margin	15	14	16	8	6	6	9	5	5	7
Net Profit	97.4%	97.2%	96.9%	91.5%	84.4%	91.4%	93.7%	88.6%	88.1%	89.7%
Net Margin	---	---	15	8	6	5	---	---	---	---
Distr. Cash Flow	15	14	16	9	8	7	9	---	---	---

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	14	13	12	12	11	11	10	10	9	5
Total Liabilities	1	1	1	1	2	1	2	2	1	2
Partner's Equity	13	12	11	11	10	9	9	8	8	3

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	105%	104%	127%	68.4%	55.4%	54.5%	81.9%	53.1%	50.4%	95.4%
Return on Equity	115%	114%	140%	75.5%	62.3%	63.0%	96.0%	63.0%	59.6%	124%
ROIC	115%	114%	140%	75.5%	62.3%	63.0%	96.0%	63.0%	59.6%	124%
Shares Out.	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Revenue/Share	2.55	2.38	2.74	1.48	1.26	1.10	1.52	0.99	0.88	1.24
DCF/Share	---	---	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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