



San Juan Basin Royalty Trust (SJT)

Updated September 5th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	\$12.00	5 Year CAGR Estimate:	-2.4%	Market Cap:	\$550 M
Fair Value Price:	\$11	5 Year Growth Estimate:	-12.0%	Ex-Dividend Date:	8/30/22
% Fair Value:	109%	5 Year Valuation Multiple Estimate:	-1.7%	Div. Payment Date:	9/15/22
Dividend Yield:	11.5%	5 Year Price Target	\$5.80	Years Of Dividend Growth:	2
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Sell

Overview & Current Events

San Juan Basin Royalty Trust (SJT) is a medium sized gas trust (it produces a negligible amount of oil), set up 40 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 \$37.6 million in 2021, and has a current market capitalization of \$550 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-August, SJT reported (8/15/2022) financial results for the second quarter of fiscal 2022. Thanks to the impressive rally of the price of natural gas, which has resulted from the sanctions of the U.S. and Europe on Russia for its invasion in Ukraine, distributable income per unit grew from \$0.15 in last year's quarter to \$0.28. Moreover, the sanctions are unlikely to loosen this year and hence SJT will keep thriving in the short run. Based on distributions per unit of \$0.92 in the first 8 months of the year, we expect annual distributable income per unit around \$1.38, a 10-year high level.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
DCFU	\$0.718	\$0.783	\$1.285	\$0.365	\$0.299	\$0.840	\$0.386	\$0.174	\$0.159	\$0.77	\$1.38	\$0.73
DPU	\$0.718	\$0.783	\$1.285	\$0.365	\$0.299	\$0.840	\$0.386	\$0.174	\$0.159	\$0.77	\$1.38	\$0.73
Units¹	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 \$0.58 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 13-year high thanks to the impact of the war in Ukraine on global 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 decline by -12% per year on average over the next five years. 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 2023.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
P/DCFU	25.2	19.3	12.1	25.2	18.0	8.9	16.9	21.2	16.6	6.5	8.7	8.0
Avg. Yld.	4.0%	5.2%	8.3%	4.0%	5.6%	11.3%	5.9%	4.7%	6.0%	15.4%	11.5%	12.5%

¹ Average Weighted Unit count is in millions.

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SJT has traded at an average price-to-DCFU of 17.0 over the last decade. The trust is currently trading at a price-to-DCFU ratio of 8.7. 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 a -1.7% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

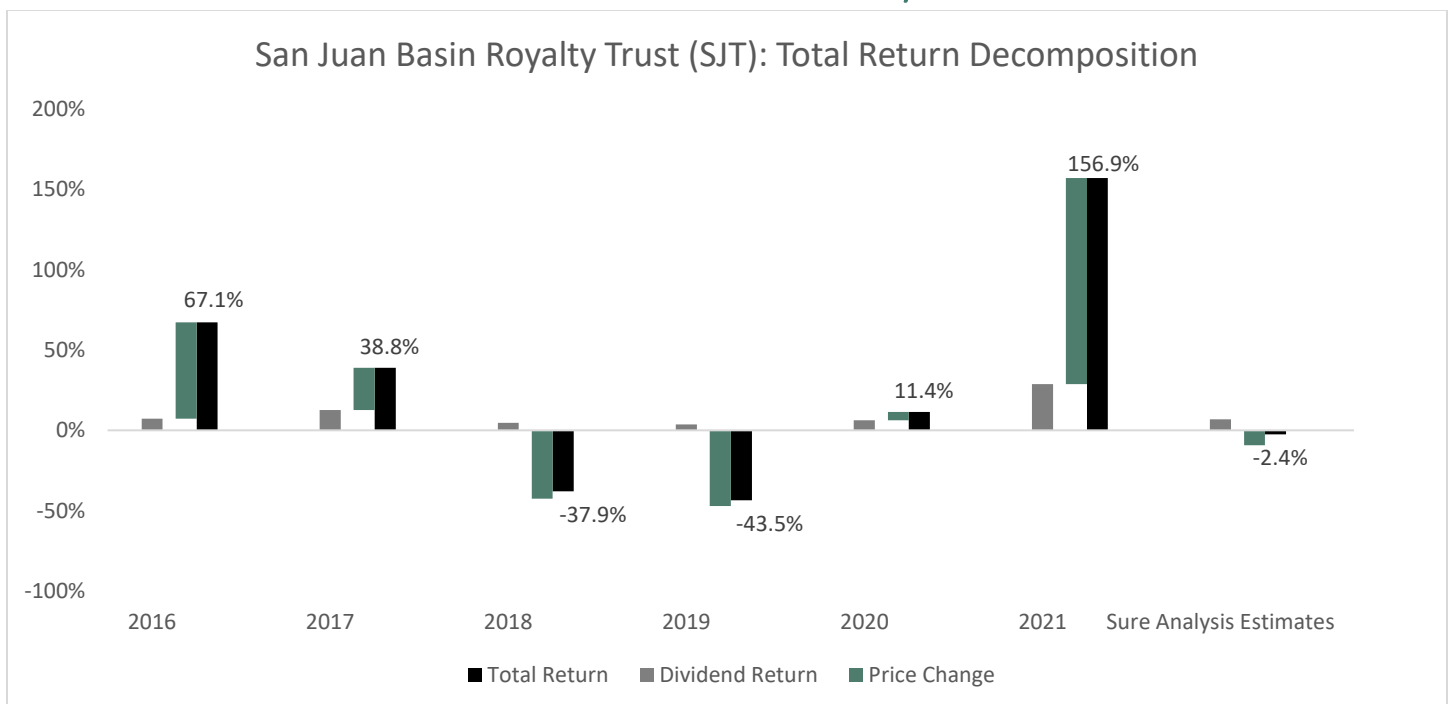
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

SJT has been in continuous existence for 40 years and has offered an average 7.0% 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 thanks to the rally of natural gas prices to a 13-year high. However, the stock has more than doubled in the last 12 months and hence it could offer a -2.4% average total return over the next five years, as its 11.5% distribution may be offset by a -12% decline of distributable income and a -1.7% valuation headwind. 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	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	35	38	62	20	18	41	19	10	9	38
SG&A Exp.	---	---	---	---	---	---	1	2	1	2
Operating Profit	35		62	20	18	41	18	8	7	36
Net Profit	33	36	60	17	14	39	18	8	7	36
Net Margin	95.5%	95.9%	97.2%	87.1%	79.5%	96.1%	92.5%	81.7%	83.9%	95.6%

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	14	16	13	11	12	11	8	7	6	10
Total Liabilities	1	5	4	2	4	4	2	1	1	6
Long-Term Debt	---	---	---	---	---	---	---	---	---	---
Partner's Equity	12	11	9	9	8	7	6	5	5	4

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	198%	250%	413%	142%	125%	345%	190%	112%	115%	440%
Return on Equity	265%	316%	589%	188%	169%	545%	289%	143%	140%	816%
ROIC	265%	316%	589%	188%	169%	545%	289%	143%	140%	816%
Shares Out.	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6	46.6
Revenue/Share	0.75	0.82	1.32	0.42	0.38	0.87	0.42	0.21	0.19	0.81

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

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