



Magellan Midstream Partners (MMP)

Updated August 5th, 2023 by Aristofanis Papadatos

Key Metrics

Current Price:	\$64	5 Year CAGR Estimate:	9.5%	Market Cap:	\$12.9 B
Fair Value Price:	\$68	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	8/4/2023
% Fair Value:	94%	5 Year Valuation Multiple Estimate:	1.3%	Dividend Payment Date:	8/14/2023
Dividend Yield:	6.5%	5 Year Price Target	\$79	Years Of Dividend Growth:	22
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Buy

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 65% of its total operating income while the transportation and storage of crude oil generates 35% of its operating income. MMP has a fee-based model; only ~9% 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 and throughout the pandemic. MMP has a market capitalization of \$12.9 billion.

During the last decade, MMP has invested about \$6 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 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 dilute unitholders and maintains a healthy payout ratio. All these attributes confirm the discipline of its management, which invests only in high-return projects.

On May 14th, 2023, MMP agreed to be acquired by Oneok (OKE) in a cash-and-stock deal. The unitholders of MMP will receive \$25 per share in cash and 0.667 shares of Oneok for every unit of MMP they own. Energy Income Partners, a major unitholder of MMP, urged the other unitholders to vote against the deal but MMP is confident that the deal will be approved in the special meeting that will take place on September 21st, 2023 and will close before year end.

In early August, MMP reported (8/3/23) financial results for the second quarter of fiscal 2023. Distributable cash flow grew 37% over the prior year's quarter thanks to tariff hikes and sustained demand for the assets of the company. MMP slightly raised its guidance for its distributable cash flow (DCF) in 2023, from \$1.22 billion to \$1.26 billion. Accordingly, we have raised our annual forecast for DCF per share from \$6.00 to \$6.20.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
CF/S	\$3.20	\$4.42	\$4.34	\$4.31	\$4.68	\$4.84	\$5.67	\$4.66	\$5.22	\$5.38	\$6.20	\$7.19
DPS	\$2.10	\$2.51	\$2.92	\$3.25	\$3.52	\$3.80	\$4.04	\$4.11	\$4.13	\$4.16	\$4.19	\$4.40
Units¹	226.7	226.7	227.4	227.8	228.0	229.1	228.7	224.0	214.1	206.1	200.0	190.0

MMP has decent growth prospects, as it has some growth projects under way. The company invested \$1.0 billion in these projects in 2019, \$355 million in 2020 and \$73 million in 2021. 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. In addition, share repurchases may constitute another significant growth driver. The only caveat is the relatively low investment in new growth projects lately (\$83 million in 2022 and expected \$110 million in 2023). However, the energy market is recovering strongly from the pandemic, with U.S. oil production close to new all-time highs. MMP has grown its cash flow per share at a 5.9% average annual rate over the last decade. In order to be on the safe side, we expect 3% annual growth in distributable cash flow per share. We also expect the aforementioned pending takeover of MMP by Oneok to materialize until the end of this year, despite the opposition of a major unitholder.

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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
P/CF	19.8	18.7	15.7	17.6	15.2	13.7	11.0	9.4	9.0	9.3	10.3	11.0
Avg. Yld.	3.9%	3.2%	4.0%	4.7%	4.9%	5.7%	6.4%	9.4%	8.8%	8.4%	6.5%	5.6%

MMP is trading at a price-to-cash flow ratio of 10.3, which is much lower than the 10-year average ratio of 13.9 of the stock. In order to be conservative, we assume a fair price-to-cash flow ratio of 11.0 for this MLP. This valuation level is in line with our expected 5-year price target of Oneok, which is in the process of acquiring MMP. If MMP trades at its fair valuation level in five years, it will enjoy a 1.3% annualized boost to total returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	65.6%	56.8%	67.3%	75.4%	75.2%	78.5%	71.2%	88.2%	79.1%	77.3%	67.6%	61.3%

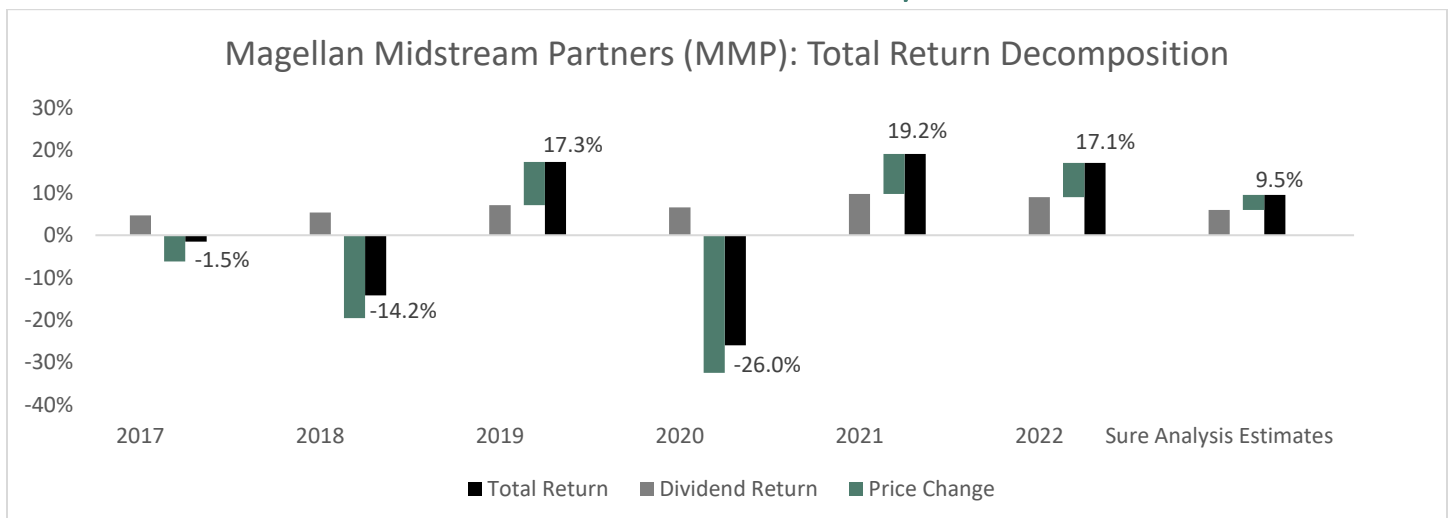
The competitive advantage of MMP comes from its fee-based model, its great scale and its discipline to invest only in high-return projects. MMP grew its dividend for 70 consecutive quarters before the freeze in 2020 and has raised its annual dividend at a 10% average annual rate since 2001. This record is a testament to the strength of the business model and the great discipline of management. Moreover, instead of issuing new shares to fund growth projects, like nearly all the MLPs, MMP repurchased its shares at low prices in 2021-2022 to enhance shareholder value. Thanks to its fee-based model, MMP proved resilient in the downturn of the oil market in 2014-2016.

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 2020, earnings fell -20% due to the pandemic but MMP has now recovered from that downturn.

Final Thoughts & Recommendation

MMP is one of the safest and highest-quality MLPs and one of the most resilient oil companies to downturns. Nearly all the oil companies posted losses or depressed profits in 2020 but MMP incurred just a ~20% decrease. MMP has rallied 16% since our last research report, in May, but it could still offer a 9.5% average annual return over the next five years thanks to its 6.5% distribution yield, 3.0% growth of cash flow per share and a potential 1.3% valuation tailwind. As the stock is trading at a 6.6% discount to its acquisition price and is offering a high yield, we maintain our buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	1,948	2,360	2,188	2,205	2,508	2,827	2,601	2,322	2,733	3,200
Gross Profit	1,227	1,604	1,574	1,534	1,675	1,857	1,809	1,611	1,725	1,788
Gross Margin	63.0%	68.0%	71.9%	69.6%	66.8%	65.7%	69.6%	69.4%	63.1%	55.9%
SG&A Exp.	132	148	150	147	166	194	194	171	206	241
D&A Exp.	142	162	167	178	197	265	231	243	228	293
Operating Profit	699	955	901	858	932	1,013	1,002	852	952	961
Operating Margin	35.9%	40.5%	41.2%	38.9%	37.2%	35.9%	38.5%	36.7%	34.8%	30.0%
Net Profit	582	840	819	803	870	1,334	1,021	817	982	1,036
Net Margin	29.9%	35.6%	37.4%	36.4%	34.7%	47.2%	39.2%	35.2%	35.9%	32.4%
Free Cash Flow	352	744	449	299	573	801	397	683	1,048	966
Income Tax	5	5	2	3	4	0	1	3	2	3

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	4,821	5,501	6,042	6,772	7,394	7,748	8,438	8,197	8,030	7,708
Cash & Equivalents	25	17	29	15	161	218	58	13	2	2
Accounts Receivable	116	84	84	106	139	104	125	104	135	220
Inventories	187	158	131	134	182	186	184	158	281	356
Goodwill & Int. Ass.	61	58	55	105	106	104	101	95	93	91
Total Liabilities	3,173	3,633	4,020	4,680	5,265	5,104	5,723	5,893	6,130	6,023
Accounts Payable	76	97	104	77	105	139	151	98	110	108
Long-Term Debt	2,685	2,967	3,440	4,087	4,524	4,271	4,706	4,979	5,089	5,015
Shareholder's Equity	1,647	1,868	2,022	2,092	2,130	2,643	2,715	2,304	1,900	1,685

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	12.6%	16.3%	14.2%	12.5%	12.3%	17.6%	12.6%	9.8%	12.1%	13.2%
Return on Equity	36.8%	47.8%	42.1%	39.0%	41.2%	55.9%	38.1%	32.6%	46.7%	57.8%
Units Out.	226.7	226.7	227.4	227.8	228.0	229.1	228.7	224.0	214.1	209.6
Revenue/Share	8.58	10.37	9.60	9.67	10.98	12.37	11.92	10.76	12.43	15.27
FCF/Share	1.55	3.27	1.97	1.31	2.51	3.50	1.65	2.96	4.77	4.61

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

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