

August 9, 2011

**Stock Rating:**
**OUTPERFORM**

12-18 mo. Price Target	\$30.00
TLLP - NASDAQ	\$21.34

3-5 Yr. EPS Gr. Rate	NA
52-Wk Range	\$25.67-\$21.00
Shares Outstanding	14.9M
Float	12.8M
Market Capitalization	\$644.6M
Avg. Daily Trading Volume	122,192
Dividend/Div Yield	\$1.35/6.33%
Fiscal Year Ends	Dec
Book Value	\$4.22
2011E ROE	NA
LT Debt	\$50.0M
Preferred	NA
Common Equity	\$86M
Convertible Available	No

DCFPU	Q1	Q2	Q3	Q4	Year	Mult.
2011E	--	0.29A	0.38	0.41	1.08	19.8x
Prior (E)	--	0.32	0.37	0.37	1.06	20.1x
2012E	0.42	0.44	0.50	0.53	1.89	11.3x
Prior (E)	0.37	0.39	0.42	0.44	1.61	13.3x
2013E	--	--	--	--	2.18	9.8x
Prior (E)	--	--	--	--	1.86	11.5x

EBITDA	Q1	Q2	Q3	Q4	Year	Mult.
2011E	--	10A	14	15	38	NM
Prior (E)	--	12	13	14	39	NM
2012E	15	16	20	21	71	NM
Prior (E)	14	14	17	18	63	NM
2013E	--	--	--	--	91	NM
Prior (E)	--	--	--	--	82	NM

Distribution	Q1	Q2	Q3	Q4	Year	Yield
2011E	--	0.338A	0.338	0.345	1.020	4.8%
Prior (E)	--	0.266	--	--	0.949	
2012E	0.355	0.365	0.375	0.385	1.480	6.9%
2013E	--	--	--	--	1.640	7.7%

## ENERGY/MASTER LIMITED PARTNERSHIPS

# **Tesoro Logistics Partners**

## **Weather Impacts 2Q11 but Growth Outlook Improves**

**SUMMARY**

We reiterate our Outperform rating and \$30 price target on TLLP after 2Q11 results and conference call. Do not get distracted by TLLP's weak 2Q11 results. Weakness resulted from severe weather in North Dakota that has already dissipated. TLLP seems to be executing its strategy even more effectively than previously assumed, with a reported \$14M-\$15M current EBITDA run rate. In addition, new growth projects were announced that will continue to drive results going forward. We believe the High Plains system (crude oil gathering in the Bakken) will have ample opportunity to grow volumes as the Williston basin develops. We are also optimistic that an accretive dropdown of assets from TSO will take place around the end of the year, further driving growth.

**KEY POINTS**

- **Operations impacted by severe weather.** TLLP did not quite meet our revised expectations for EBITDA or DCFPU during the quarter. We anticipated the weather effects but underestimated the extent. Pro rata EBITDA was \$10.4M vs. our \$11.5M estimate. Importantly, the distribution was in line with our estimate and reflects the MQD run rate, or \$0.3375.
- **Weather effects already dissipated.** North Dakota's severe weather will continue to impact results into 3Q11 but as of early August, volumes on the High Plains system had rebounded to the 60,000 bpd range, signifying a return to previous levels.
- **EBITDA run-rate higher than expected.** Mgmt reported that the current EBITDA run-rate is between \$14M & \$15M. Our previous model assumed \$14M in 4Q11. TLLP appears to be executing its business strategy more rapidly than previously believed. We are raising estimates to reflect this new data.
- **New growth projects announced.** New projects were announced both on the High Plains system and in terminalling. We expect \$10M of incremental EBITDA from TLLP's slate of organic growth projects. We also suspect that, given strong growth in the Bakken, there is much more to come on High Plains.
- **Dropdown from TSO expected in next 2-3 quarters.** TLLP has rights of first offer (ROFO) on the remainder of TSO's crude oil infrastructure assets. We expect TLLP to take advantage of this ROFO sometime around late 2011 or early 2012. We assume a \$100M acquisition at 10x EBITDA.

**Stock Price Performance**

**Company Description**

TLLP is a fee-based, growth-oriented MLP formed by Tesoro to own, operate, develop and acquire crude oil and refined products logistics assets. Assets consist of a crude oil gathering system in the Bakken Shale/Williston Basin, eight refined products terminals in the Midwest and West, and a crude oil and refined products storage facility and five related short-haul pipelines in Utah.

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Summary Financial Statements										Shawn Radtke (720) 554-1101	
Millions of Dollars Except for Per Unit Amounts											
Fiscal Year Ending December 31,											
Summary Income Statement	2010A	2011Q2A	2011Q3E	2011Q4E	2011E	2012Q1E	2012Q2E	2012Q3E	2012Q4E	2012E	2013E
Crude Oil Gathering	50	10.7	14.0	14.6	39.3	14.8	15.7	17.8	18.6	66.9	72.9
Terminalling, transportation and storage	44	9.1	11.1	12.0	32.2	12.4	13.1	14.1	14.6	54.2	60.6
Total Revenues	93	19.8	25.1	26.6	71.5	27.2	28.8	31.9	33.2	121.0	133.5
Operating expenses											
Operating and maintenance expense	37	8.1	9.7	10.3	28.2	10.6	11.2	12.4	13.0	47.2	52.1
Depreciation expense	8	2.0	2.5	2.7	7.2	2.7	2.9	3.2	3.3	12.1	13.4
General and administrative expense	3	2.1	1.6	1.6	5.2	1.7	1.8	2.0	2.1	7.6	8.3
Total operating expenses	48	12.2	13.8	14.6	40.6	15.0	15.9	17.6	18.4	66.9	73.8
Operating income	45	7.5	11.3	12.0	30.9	12.2	12.9	14.3	14.9	54.2	59.8
Interest Expense	2	0.5	0.4	0.4	1.2	0.8	0.8	2.2	2.2	6.1	13.3
Income before income taxes	42	7.1	10.9	11.7	29.7	11.3	12.0	12.0	12.6	48.0	46.5
Interest Expense	2	0.5	0.4	0.4	1.2	0.8	0.8	2.2	2.2	6.1	13.3
Net income	42	7.1	10.9	11.7	29.7	11.3	12.0	12.0	12.6	48.0	46.5
Less: Allocations to GP	1	0.1	0.2	0.2	0.6	0.2	0.3	0.3	0.3	1.1	1.1
Net Income allocable to LP	42	6.9	10.7	11.4	29.0	11.1	11.8	11.8	12.3	47.0	45.3
Earnings Per LP Unit	1.34	0.22	0.34	0.37	0.93	0.36	0.38	0.38	0.40	1.51	1.46
Distributable Cash Flow Calculation	2010A	2011Q2A	2011Q3E	2011Q4E	2011E	2012Q1E	2012Q2E	2012Q3E	2012Q4E	2012E	2013E
Net Income	42	7.1	10.9	11.7	29.7	11.3	12.0	12.0	12.6	48.0	46.5
Depreciation Expense	8	2.0	2.5	2.7	7.2	2.7	2.9	3.2	3.3	12.1	13.4
Interest Expense	2	0.5	0.4	0.4	1.2	0.8	0.8	2.2	2.2	6.1	13.3
EBITDA	53	9.6	13.8	14.7	38.1	14.9	15.8	17.5	18.2	66.3	73.1
Dropdown Addition to EBITDA	0	0.0	0.0	0.0	0.0	0.0	0.0	2.5	2.5	5.0	17.5
Adjusted EBITDA	53	9.6	13.8	14.7	38.1	14.9	15.8	20.0	20.7	71.3	90.6
Cash Interest	2	0.0	0.2	0.2	0.5	0.6	0.6	2.4	2.4	6.1	14.5
Cash Taxes	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Maintenance Capex	2	0.3	1.4	1.5	3.2	1.0	1.1	1.6	1.7	5.4	7.2
Other	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Distributable Cash Flow	49	9.2	12.2	13.0	34.4	13.2	14.0	15.9	16.6	59.8	68.8
Total DCF / Unit	1.57	0.30	0.39	0.42	1.11	0.42	0.45	0.51	0.53	1.92	2.21
GP distribution	0.00	0.01	0.01	0.01	0.02	0.01	0.01	0.01	0.01	0.03	0.03
DCF / LP unit	1.57	0.29	0.38	0.41	1.08	0.42	0.44	0.50	0.53	1.89	2.18
LP distribution / Unit		0.3375	0.3375	0.3450	1.0200	0.3550	0.3650	0.3750	0.3850	1.4800	1.6400
LP distribution / Growth						8%	11%	12%		45%	11%
Coverage		0.9x	1.1x	1.2x	1.1x	1.2x	1.2x	1.3x	1.4x	1.3x	1.3x
Summary Statement of Cash Flow	2010A	2011Q2E	2011Q3E	2011Q4E	2011E	2012Q1E	2012Q2E	2012Q3E	2012Q4E	2012E	2013E
Cash Flow From Operations	0	9.6	13.6	14.5	37.6	14.2	15.1	15.0	15.8	60.2	58.6
Capital Expenditures	0	(4.8)	(5.9)	(6.0)	(16.7)	(3.0)	(3.1)	(3.6)	(3.7)	(13.4)	(15.2)
Sales (Purchases) of Assets	0	0.0	0.0	0.0	0.0	0.0	0.0	(100.0)	0.0	(100.0)	(100.0)
Cash Flow From Investing	0	(4.8)	(5.9)	(6.0)	(16.7)	(3.0)	(3.1)	(103.6)	(3.7)	(113.4)	(115.2)
Distributions	0	(10.7)	(10.7)	(11.0)	(32.4)	(11.3)	(11.6)	(11.9)	(12.2)	(47.0)	(50.6)
Net Equity Issuance	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Debt Issuance	0	6.0	3.0	2.5	11.5	0.1	(0.4)	100.5	0.1	100.3	107.2
Cash Flow From Financing	0	(4.7)	(7.7)	(8.5)	(20.9)	(11.2)	(12.0)	88.6	(12.1)	53.2	56.7
Summary Balance Sheet	2010A	2011Q2E	2011Q3E	2011Q4E	2011E	2012Q1E	2012Q2E	2012Q3E	2012Q4E	2012E	2013E
Cash	3	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Total Current Assets	3	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Net PP&E	132	136.4	142.3	148.3	148.3	151.3	154.4	258.0	261.7	261.7	376.9
Total Assets	137	141.4	147.3	153.3	153.3	156.3	159.4	263.0	266.7	266.7	381.9
Short-Term Debt	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Current Liabilities	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Long-Term Debt	50	56.0	59.0	61.5	61.5	61.6	61.1	161.6	161.7	161.7	269.0
Total Liabilities	50	56.0	59.0	61.5	61.5	61.6	61.1	161.6	161.7	161.7	269.0
Total Equity	87	85.4	88.3	91.8	91.8	94.8	98.3	101.4	104.9	104.9	113.0
Total Liabilities & Equity	137	141.4	147.3	153.3	153.3	156.3	159.4	263.0	266.7	266.7	381.9
Operating Data	2010A	2011Q2A	2011Q3E	2011Q4E	2011E	2012Q1E	2012Q2E	2012Q3E	2012Q4E	2012E	2013E
Crude Gathering											
Pipeline Throughput (bpd)	50,695	56,635	59,467	62,440	57,848	64,938	68,185	71,594	73,742	69,614	74,297
Trucking Volume (bpd)	23,305	23,212	24,605	25,343	24,087	26,103	27,408	28,779	30,218	28,127	30,597
Terminalling, Transportation and Storage											
Terminal Throughput (bpd)	113,950	131,812	139,721	146,707	133,161	154,042	161,744	163,362	163,362	160,627	163,362
Short Haul Pipeline Volume (bpd)	60,666	66,174	72,791	76,431	69,471	77,960	79,519	80,712	81,922	80,028	82,951
Storage capacity reserved	878,000	878,000	878,000	878,000	878,000	878,000	886,000	886,000	886,000	884,000	886,000
Source: Company reports; Oppenheimer & Co. estimates; SNL. Please refer to Opco reports for more details											8/9/11

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8/9/11

## Investment Thesis

TLLP is currently our top pick within our MLP coverage. We believe TLLP represents the first opportunity in several years to own a 100% fee-based (low-risk) MLP with significant dropdown and organic growth potential early in its life cycle. We forecast double-digit distribution growth CAGR for the next several years as TLLP expands organically and completes acquisitions. Assets include a large crude oil gathering system in North Dakota and Montana that provides exposure to Bakken formation growth. We believe the Bakken is in the very early stages of development and that TLLP provides one of the most concentrated ways to invest in Bakken production.

## Price Target Calculation

Our price target of \$30 per unit is derived using our distribution discount model (DDM). The assumptions underlying this price target are stage one (years 1 & 2) growth of 10%, stage two (years 3-5) growth of 8%, a terminal growth rate of 2% and a discount rate of 8.0%. The terminal distribution is projected to be \$2.06 and is achieved in 2015.

## Key Risks to Price Target

- Weak refined product demand
- Potential to overpay for acquisition
- Acquisition integration
- Rising interest rates
- Economic weakness
- Capital markets access
- Major change in MLP tax code
- FERC regulatory risk
- Conflicts of interest between LPs and GPs
- Counterparty credit risk
- Energy infrastructure overbuild
- Extreme weather
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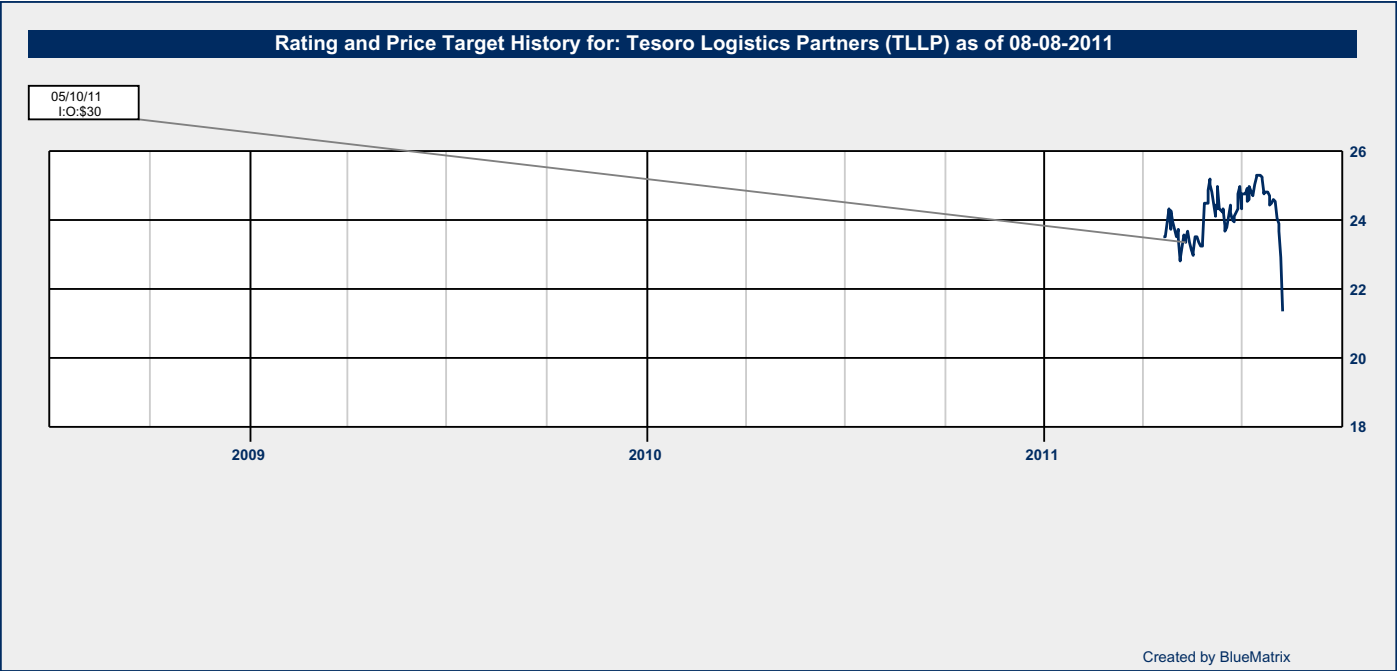
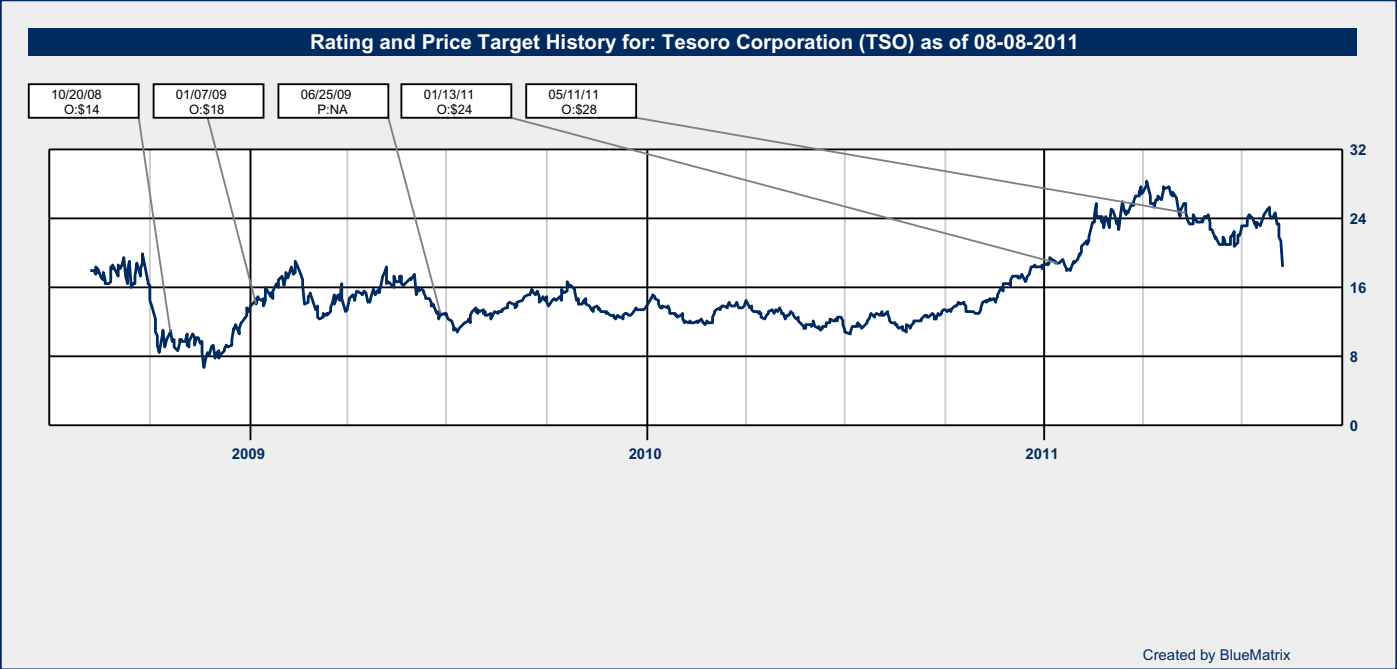
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Stock Prices as of August 9, 2011  
Tesoro Corporation (TSO - NYSE, 18.39, OUTPERFORM)



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Distribution of Ratings/IB Services Firmwide				
Rating	Count	IB Serv/Past 12 Mos.		
		Percent	Count	Percent
OUTPERFORM [O]	324	54.50	144	44.44
PERFORM [P]	260	43.80	84	32.31
UNDERPERFORM [U]	10	1.70	2	20.00

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