

**TESORO LOGISTICS LP (TLLP: \$29.01)**

December 6, 2011

**Raising Price Target**
**Rating: Buy**
**Price Target: Old - \$27.50; New - \$33.00**

Market Data					
12-18 Month Price Target					\$33.00
52-Week Range					\$29.55 - \$21.00
ADTV - 90Day (000s)					49.8
Market Cap (\$MM)					\$885.1
Shares Out (MM)					30.5
Public Market Float (MM)					13.0
Dividend					\$1.40
Dividend/Yield					4.83%
Earnings Per Unit (EPU) (\$)					
FY DEC	2011	2012		2013	
	Estimate	Previous	Current	Previous	Current
Q1	—	—	\$0.42E	\$0.53	\$0.61E
Q2	\$0.25A	\$0.47	\$0.49E	\$0.54	\$0.62E
Q3	\$0.49A	—	\$0.57E	\$0.56	\$0.63E
Q4	\$0.38E	\$0.54	\$0.56E	\$0.53	\$0.62E
YEAR	\$1.12E	\$2.00	\$2.04E	\$2.16	\$2.48E
Distribution Per Unit (\$)					
FY DEC	2011	2012		2013	
	Estimate	Previous	Current	Previous	Current
Q1	—	—	\$0.370E	\$0.410	\$0.430E
Q2	\$0.245A	—	\$0.380E	\$0.420	\$0.450E
Q3	\$0.350A	\$0.390	\$0.400E	\$0.430	\$0.470E
Q4	\$0.360E	\$0.400	\$0.410E	\$0.440	\$0.480E
YEAR	\$0.955E	\$1.540	\$1.560E	\$1.700	\$1.830E
Valuation Ratio					
		FY11	FY12	FY13	
Debt/EBITDA		1.2x	0.6x	0.5x	
EBITDA/Interest		24.8x	46.8x	58.9x	
EV/EBITDA		21.7x	11.5x	9.1x	
P/DCF		22.8x	13.1x	11.2x	
Financial Data					
		FY11	FY12	FY13	
EBITDA		\$42.2E	\$79.6E	\$100.1E	
Balance Sheet					
		FY11	FY12	FY13	
Total Assets		\$166.3E	\$286.9E	\$310.0E	
Long Term Debt		\$50.0E	\$155.0E	\$155.0E	
Total SOE and Liab.		\$166.3E	\$286.9E	\$310.0E	

**Company Description**

Tesoro Logistics is a Master Limited Partnership that gathers, transports, and stores crude oil and distributes, transports, and stores refined products. Its assets consist of a crude oil gathering system in the Bakken Shale/Williston Basin area, eight refined products terminals, and a crude oil and refined products storage facility and five related short-haul pipelines.

**Increasing Price Target on Higher Long-Term Distribution Growth Outlook**
**Summary**

Tesoro Logistics LP (TLLP) announced its updated 2012 business plan. Capital spending and an asset dropdown should help to push EBITDA above our previous estimates. We are increasing our outlook for the partnership's distribution. Because of the improved outlook, we are increasing our price target to \$33/unit from \$27.75/unit. We believe Tesoro's distribution growth should be solid over the next several years, including estimated 2013 distribution growth at 17.3%. We have a Buy rating on Tesoro's units.

**Key Points**

- **Updated 2012 plan.** Tesoro announced its 2012 business plan, which should result in 2013 EBITDA of \$100 million. The highlights of the plan are capital expenditures of \$100 million between 2012 and 2013 and the acquisition of a crude oil terminal from Tesoro Corporation (TSO-NR). The partnership plans to spend \$60 million on its High Plains System, which should continue to benefit from growth in the Bakken. Spending on the Terminals segment is budgeted at \$40 million.
- **Asset dropdown.** The partnership's first dropdown from its parent will be the Martinez Crude Oil Marine Terminal in Martinez, CA. The asset should generate \$8 million in EBITDA annually and is supported by a 10-year commitment with two five-year renewals. The transaction should close by the end of 1Q12 or the beginning of 2Q12 and should be financed with Tesoro's credit facility. The purchase price has not been disclosed yet.
- **Our take.** Our previous estimates did not include any dropdowns. The healthy capex spending and the asset acquisition should enable Tesoro to increase its distribution over the long term at a rate greater than we had modeled. After speaking with management, we are also comfortable that there are other organic growth projects the partnership will pursue and further potential asset dropdowns. We believe Tesoro could also pursue third-party acquisitions.
- **Estimates.** We are maintaining our 2011 distribution estimate at \$0.9548/unit, increasing our 2012 estimate to \$1.56/unit from \$1.54/unit and upping our 2013 estimate to \$1.83/unit from \$1.70/unit. Our estimates provide a 17.3% growth rate in 2013. Our distributable cash flow estimate are \$2.22/unit for 2012 and \$2.60/unit in 2013, which equates to coverage ratios of 1.4x for both years. Our estimates do not include any further asset dropdowns.
- **Investment thesis.** We believe Tesoro will be among the leaders in distribution growth over the next several years, including estimated 2013 distribution growth at 17.3%. In addition, the partnership should benefit from its organic growth capital spending and potential dropdown acquisitions. The partnership's assets are well-positioned to take advantage of growing production from the Bakken Shale.

**Updated 2012 Plan**

Tesoro announced its 2012 business plan, which should result in 2013 EBITDA of \$100 million. The highlights of the plan are capital expenditures of \$100 million between 2012 and 2013 and the acquisition of a crude oil terminal from Tesoro Corporation.

The partnership plans to spend \$60 million on its High Plains System, which should continue to benefit from growth in the Bakken. This system should realize benefits from growth at Tesoro Corporation's Mandan and Anacortes refineries. In addition, the partnership is expanding its trucking fleet to increase volumes. Capital spending should total \$60 million, which should result in an EBITDA contribution of \$20 million to \$25 million. The capital spending includes some previously announced projects.

Spending on the Terminals segment is budgeted at \$40 million, which should lead to an EBITDA contribution of \$5 million to \$10 million. The partnership's goal is to grow terminalling volumes over 40,000 barrels per day by the end of 2013.

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**Distribution**

We are maintaining our 2011 distribution estimate at \$0.9548/unit, increasing our 2012 estimate to \$1.56/unit from \$1.54/unit and upping our 2013 estimate to \$1.83/unit from \$1.70/unit. Our estimates provide a 17.3% growth rate in 2013. Our distributable cash flow estimate are \$2.22/unit for 2012 and \$2.60/unit in 2013, which equates to coverage ratios of 1.4x for both years. Our estimates do not include any further asset dropdowns.

**Estimates**

We are keeping our 2011 EBITDA estimate at \$42.2 million and increasing our 2012 EBITDA estimate to \$79.6 million from \$72.8 million. We are maintaining our 2011 DCF estimate at \$39.5 million upping our 2012 DCF estimate to \$69.4 million from \$67.1 million.

Figure 1 – Tesoro Logistics – Model

\$ in millions except per unit data	1Q11	2Q11	3Q11	4Q11E	2011E	1Q12E	2Q12E	3Q12E	4Q12E	2012E	1Q13E	2Q13E	3Q13E	4Q13E	2013E
Operating Income	-	7.5	15.7	12.4	35.7	13.8	16.8	19.5	19.4	69.5	21.1	21.7	22.0	21.8	86.7
Interest expense, net	-	(0.5)	(0.6)	(0.6)	(1.7)	(0.8)	(1.6)	(1.7)	(1.9)	(5.950)	(1.9)	(1.9)	(1.9)	(1.9)	(7.5)
Other income	-	0.8	0.0	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pre-tax income	-	7.9	15.1	11.8	34.9	13.0	15.2	17.8	17.5	63.5	19.2	19.9	20.2	19.9	79.2
Income Tax	-	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Income	-	7.9	15.1	11.8	34.9	13.0	15.2	17.8	17.5	63.5	19.2	19.9	20.2	19.9	79.2
Net Income to General Partner	-	0.2	0.3	0.2	0.7	0.3	0.3	0.4	0.5	1.4	0.6	0.8	1.0	1.1	3.5
Net Income to Limited Partners	-	7.7	14.8	11.6	34.2	12.7	14.9	17.4	17.1	62.1	18.6	19.0	19.2	18.8	75.7
<b>Net Income/Unit (Limited)</b>	-	<b>\$0.25</b>	<b>\$0.49</b>	<b>\$0.38</b>	<b>\$1.12</b>	<b>0.42</b>	<b>\$0.49</b>	<b>\$0.57</b>	<b>\$0.56</b>	<b>\$2.04</b>	<b>0.61</b>	<b>\$0.62</b>	<b>\$0.63</b>	<b>\$0.62</b>	<b>\$2.48</b>
Limited Partnership Units	-	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5
<b>EBITDA (total)</b>	-	10.0	17.7	14.5	42.2	15.8	19.4	22.2	22.2	79.6	24.4	25.1	25.5	25.2	100.1
EBITDA (Limited Partners)	-	9.9	17.4	14.2	41.5	15.5	19.1	21.8	21.8	78.2	23.8	24.3	24.5	24.1	96.6
Other	-	(0.0)	(0.3)	(0.4)	(0.7)	(0.5)	(0.9)	(1.0)	(1.1)	(3.6)	(1.8)	(1.8)	(1.8)	(1.8)	(7.1)
Maintenance CAPEX	-	(0.3)	(0.3)	(1.5)	(2.1)	(1.2)	(1.1)	(2.1)	(2.1)	(6.6)	(2.3)	(2.3)	(2.3)	(2.3)	(9.4)
Distributable Cash Flow	-	9.7	17.2	12.6	39.5	14.1	17.3	19.0	19.0	69.4	20.3	21.0	21.4	21.1	83.7
Distributable Cash Flow (GP)	-	(0.2)	(0.3)	(0.3)	(0.8)	(0.3)	(0.3)	(0.5)	(0.5)	(1.6)	(0.8)	(1.0)	(1.3)	(1.4)	(4.4)
Distributable Cash Flow (LP)	-	9.5	16.8	12.3	38.7	13.8	17.0	18.6	18.5	67.8	19.5	19.9	20.1	19.7	79.3
<b>Distributable Cash Flow/Unit</b>	-	<b>\$0.31</b>	<b>\$0.55</b>	<b>\$0.40</b>	<b>\$1.27</b>	<b>0.45</b>	<b>\$0.56</b>	<b>\$0.61</b>	<b>\$0.60</b>	<b>\$2.22</b>	<b>0.64</b>	<b>\$0.65</b>	<b>\$0.66</b>	<b>\$0.65</b>	<b>\$2.60</b>
<b>Distribution</b>		\$0.2448	\$0.3500	\$0.3600	<b>\$0.9548</b>	\$0.3700	\$0.3800	\$0.4000	\$0.4100	<b>\$1.5600</b>	\$0.4300	\$0.4500	\$0.4700	\$0.4800	<b>\$1.8300</b>
<b>Coverage Ratio</b>					<b>1.3x</b>					<b>1.4x</b>					<b>1.4x</b>
Distribution Growth															<b>17.3%</b>
Debt/EBITDA										<b>1.9x</b>					<b>1.5x</b>
EBITDA/Interest Expense										<b>13.4x</b>					<b>13.4x</b>

Source: Partnership reports and Wunderlich Securities, Inc. estimates

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### Valuation/Risks

- We have a Buy rating on TLLP and a \$33 price target. Our price target is derived through a two-stage distribution discount model, which assumes a required rate of return of 8% and a long-term growth rate of 2.0%. Our terminal value in 2016 is \$38.08.
- MLPs are tax-advantaged investments. Congress or the IRS could decide to remove these tax benefits. This is the biggest risk to all MLPs.

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Ratings Distribution & Investment Banking Disclosure				
Rating	Count	Ratings Distribution*	Count	Investment Banking**
Buy -rated	138	62.40	18	13.04
Hold -rated	80	36.20	7	8.75
Sell -rated	3	1.40	0	0.00

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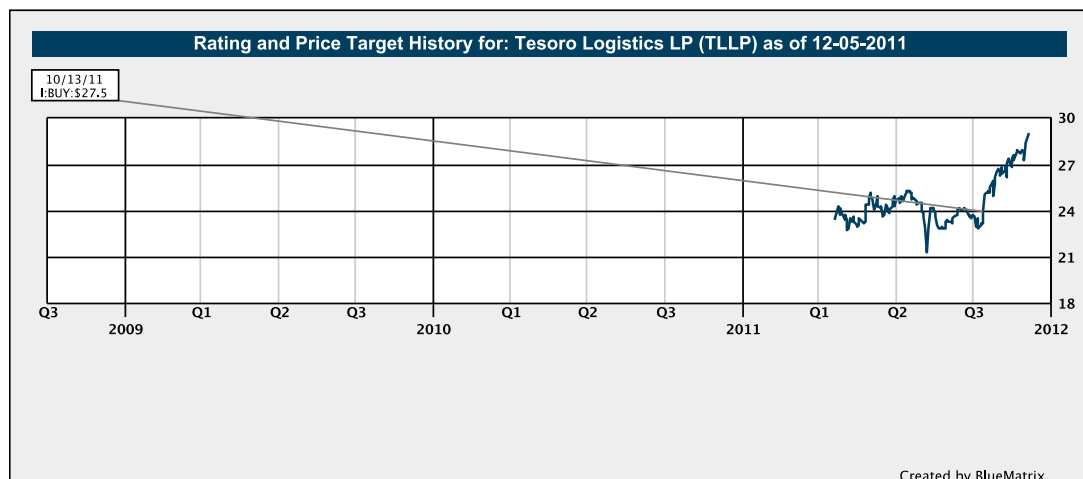
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