November MLP Market Update & News

Earnings season begins, IDRs near elimination, and a look back at the last time energy equities were out of favor

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MLP Market Overview

Midstream master limited partnerships (MLPs), as measured by the Alerian MLP Index (AMZ), ended October down 7.4% on a price basis and down 6.3% once distributions are considered. The AMZ results underperformed the S&P 500 Index's 2.2% total return for the month. The best performing midstream subsector for October was the Marine group, while the Propane subsector underperformed, on average.

For the year through October, the AMZ is down 3.1% on a price basis, resulting in a 3.9% total return. This compares to the S&P 500 Index's 21.2% and 23.2% price and total returns, respectively. The Compression group has produced the best average total return year-to-date, while the Gathering and Processing subsector has lagged.

MLP yield spreads, as measured by the AMZ yield relative to the 10-Year U.S. Treasury Bond, widened by 65 basis points (bps) over the month, exiting the period at 764 bps. This compares to the trailing five-year average spread of 542 bps and the average spread since 2000 of approximately 380 bps. The AMZ indicated distribution yield at month-end was 9.3%.

Midstream MLPs and affiliates raised no new marketed equity (common or preferred, excluding at-the-market programs) or debt over the month. MLPs and affiliates announced $6.2 billion new asset acquisitions in October, including a major acquisition tied to an MLP simplification.

Spot West Texas Intermediate (WTI) crude oil exited the month at $54.18 per barrel, up 0.2% over the period and 17.0% lower year-over-year. Spot natural gas prices ended October at $2.73 per million British thermal units (MMbtu), up 15.2% over the month but 17.5% lower than October 2018. Natural gas liquids (NGL) pricing at Mont Belvieu exited the month at $22.01 per barrel, 11.3% higher than the end of September and 28.7% lower than the year-ago period.

News

Third Quarter Earnings Season Begins. Third quarter reporting season kicked-off in October. Through month-end, 51 midstream entities had announced distributions for the quarter, including 19 distribution increases and 32 distributions that were unchanged from the previous quarter. Through the end of October, 22 sector participants had reported third quarter financial results. Operating performance has been, on average, modestly below expectations with EBITDA, or Earnings Before Interest, Taxes, Depreciation and Amortization, coming in 1.0% lower than consensus estimates but 3.0% higher than the preceding quarter.

Another MLP Simplification Moves Forward. Hess Midstream (NYSE: HESM) announced an agreement to acquire Hess Infrastructure Partners LP (HIP), including HIP's outstanding economic general partner interest and incentive distribution rights (IDRs) in HESM. In addition, HESM will be converted into an "Up-C" structure in which IDR payments to sponsors are eliminated. Once the HESM transaction is completed only 17 midstream entities with IDRs will remain:

Blueknight Energy (NYSE: BKEP)
BP Midstream (NYSE: BPMP)
CNX Midstream (NYSE: CNXM)
CrossAmerica Partners (NYSE: CAPL)
CSI Compressco (NYSE: CCLP)
DCP Midstream (NYSE: DCP)
Delek Logistics Partners (NYSE: DKL)
Enable Midstream (NYSE: ENBL)
Global Partners (NYSE: GLP)
Martin Midstream (NYSE: MMLP)
Noble Midstream (NYSE: NBLX)
Oasis Midstream (NYSE: OMP)
Shell Midstream (NYSE: SHLX)
Summit Midstream (NYSE: SMLP)
Sunoco (NYSE: SUN)
TC Pipeline (NYSE: TCP)
USD Partners (NYSE: USDP)

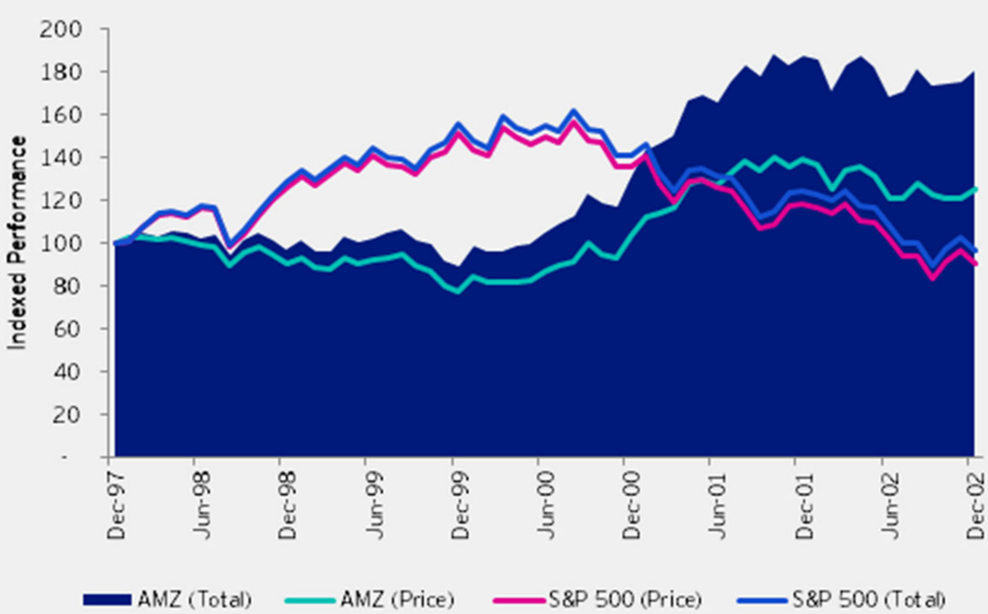
Private Equity Continues to Show Interest in Energy Infrastructure. Brookfield Super-Core Infrastructure Partners acquired a 25% equity stake in Cove Point LNG from Dominion (NYSE: D) for $2 billion. Cove Point owns a liquefied natural gas (LNG) import, export and storage facility on the Maryland coast, including a 136-mile pipeline that interconnects the facility with the interstate pipeline system. These assets provide liquefaction, gasification, transportation, storage and peaking gas supply services to customers in the United States, India and Japan.

Chart of the Month

Energy equities remain out of favor. The energy weighting within the S&P 500 Index has hit an all-time low of 4.3% versus the twenty-year average of 8.6%. We believe investor apathy has also impacted midstream fund flows and, as a result, price realization for sector participants. MLPs now trade at an EV/EBITDA multiple of 9.6x and yield 9.3% versus the 10-year average of 12.5x and 7.0%, respectively. Midstream trading weakness has persisted despite continued healthy operating performance and an average distribution coverage ratio that is at an all-time high. However, this is not the first time midstream equities have suffered from investor apathy.

Between the fall of 1998 and the summer of 2000, the broader equity market, as measured by the S&P 500 Index, rose 60% and the Nasdaq soared 180%. Tech stocks were providing such great returns that other sectors struggled to gain interest. Over this period, MLPs, as measured by the Alerian MLP Index, only gained 3%; drastically underperforming, even though crude oil prices had rallied 150% over the same period. However, it should be pointed out, after considering the distributions received, MLP total return over this period neared 20%. This relative underperformance reversed in 2000 when tech and the broader market began to falter. Between late summer 2000 and the fall of 2002, the S&P 500 Index declined 50% and the Nasdaq lost 75%, while the Alerian MLP Index appreciated by 25% and provided a 45% total return, once factoring in distributions.

Exhibit: Tech Bubble Period Performance



Source: Bloomberg. Past performance does not guarantee future results.

DISCLOSURES

Source: Bloomberg LP, for all historical data.

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The Alerian MLP Index is a float-adjusted, capitalization-weighted index measuring master limited partnerships, whose constituents represent approximately 85% of total float-adjusted market capitalization. The S&P 500 Index is a broad-based measure of domestic stock market performance. Indices are unmanaged and cannot be purchased directly by investors. Index performance is shown for illustrative purposes only and does not predict or depict the performance of any investment. Past performance does not guarantee future results.

Investing in MLPs involves additional risks as compared to the risks of investing in common stock, including risks related to cash flow, dilution and voting rights. Each fund's investments are concentrated in the energy infrastructure industry with an emphasis on securities issued by MLPs, which may increase volatility. Energy infrastructure companies are subject to risks specific to the industry such as fluctuations in commodity prices, reduced volumes of natural gas or other energy commodities, environmental hazards, changes in the macroeconomic or the regulatory environment or extreme weather. MLPs may trade less frequently than larger companies due to their smaller capitalizations which may result in erratic price movement or difficulty in buying or selling. Additional management fees and other expenses are associated with investing in MLP funds. Diversification does not guarantee profit or protect against loss.

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