



## AND THE ELECTION WINNER IS...MLPS

# MLPs Poised to Benefit from an Improving Outlook

DECEMBER 2016

MLPs are positioned for a sustained recovery in 2017 and beyond. Our outlook for MLPs has steadily improved throughout 2016 as sector and market conditions have improved. The latest positive developments, namely the election of Donald Trump and OPEC's decision to support oil prices with a production cut, have only increased our favorable outlook for MLPs.

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Portfolio Manager,  
Midstream and MLPs

### POSITIVE IMPLICATIONS OF THE TRUMP PRESIDENCY

The outcome of the U.S. presidential election represents a significant positive event for the U.S. energy industry with several positive implications for MLPs. Specific to the energy sector, Donald Trump (1) is a proponent of utilizing U.S. fossil fuel energy resources, (2) has outlined a large infrastructure spending plan that includes energy infrastructure,

and (3) plans to reduce regulations impacting the energy industry.

More broadly, Trump plans to reduce taxes and increase spending to stimulate economic activity and growth in the U.S. Accelerating economic growth could lead to an acceleration of demand for oil and natural gas, which is a positive for assets owned by MLPs.

The combination of these policy goals represents a positive backdrop for energy infrastructure projects by providing an improved regulatory and political climate that incentivizes investment.

#### THE "TRUMP FACTOR"

The new administration plans to expand U.S. oil and natural gas production, while also supporting an increase in infrastructure spending across sectors. Further policies to eliminate restrictions on oil drilling and natural gas exploration on federal lands to expand the availability of natural gas resources while streamlining the permitting and approval process have also been announced.

#### IMPROVING ENERGY FUNDAMENTALS

Through improved efficiencies and reduced drilling costs, U.S. producers are generating returns comparable to or better than returns they generated in higher oil price environments.

OPEC's announced production cut should further stabilize oil markets and push oil prices higher.

#### MLPS ARE ATTRACTIVELY VALUED

MLPs have emerged from their 2015 price declines much healthier with improved leverage and cash flow sustainability.

MLPs are "on sale" trading at a discount to historical averages. Valuations are compelling with cash flow multiples at the low end of the range versus history, more than 7.5% yield and 3-5% annual distribution growth.

## MLP OUTLOOK CONTINUES TO IMPROVE

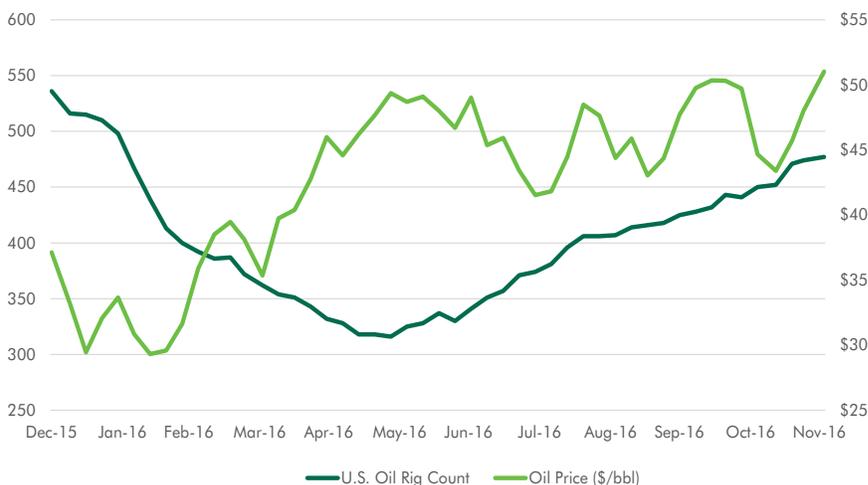
Outside of the positive impacts of the surprise election, the outlook for MLPs has steadily improved throughout 2016.

### OIL PRICE RECOVERY AND OPEC

Oil prices bottomed in February and have rallied nearly 100%. The market established a range of \$40-\$50/bbl for much of the year, supported by a clear shift in tone from The Organization of the Petroleum Exporting Countries (OPEC) and Russia starting in late summer 2016. In Q4 2016, OPEC announced a production cut that may push that range higher to \$50-60/bbl, and raises confidence in a floor for oil price of at least \$45/bbl (Exhibit 1). OPEC nations depend on oil revenues to fund social programs and federal budgets. OPEC's change in tone is an admission that its original plan to let lower prices reduce global production without intervention failed, in part because of the resilience of non-OPEC production from the U.S. and Russia. A floor for global oil prices at \$45/bbl is very significant for the outlook for U.S. production growth and by extension, provides a clear path to growth for the MLP sector.

U.S. producers have improved efficiencies and reduced drilling costs so dramatically in 2015 and 2016 that they are able to generate returns on development comparable or better than returns they used to generate in a much higher oil price environment. MLPs benefit from growth in production, because it results in higher utilization of existing energy infrastructure (pipelines, storage tanks, processing plants), and leads to opportunities to develop new infrastructure.

EXHIBIT 1: OIL PRICE FLUCTUATION AND STEADY OIL RIG COUNT INCREASE



Source: CBRE Clarion Securities, Baker Hughes, and FactSet as of 12/2/2016. Please refer to Important Disclosures on the back page for additional information.

### SELF-HELP

Under pressure from credit ratings agencies and investors, MLPs have taken constructive action to improve leverage and cash flow sustainability, with more transactions expected in 2017. MLPs have reduced distributions, sold assets, executed joint venture agreements for ownership of assets and development projects, reduced capital expenditures, and renegotiated contracts with producers. These actions have put MLPs on a healthier footing with lower leverage and higher retained cash flow.

### CAPITAL MARKET ACCESS

Due to "self-help", MLPs have re-established access to equity capital markets throughout 2016, raising more than \$15bn in common and preferred equity, helped by strong positive fund flows into MLP-related vehicles. Also, credit spreads for MLPs steadily improved as pressure on the energy sector subsided, allowing MLPs to access the debt capital markets as well. A major driver of the decline in MLP prices in 2015 and early 2016 was uncertainty around capital market access for MLPs that have generally relied almost exclusively on external funding for growth over the years. As oil prices stabilized and energy capital markets began to open up, MLPs did their best to reduce spending plans and limit their capital needs. MLPs emerged healthier with less of a need to access the capital markets while the capital markets loosened, the combination of which helped MLPs recover from lows early in 2016.



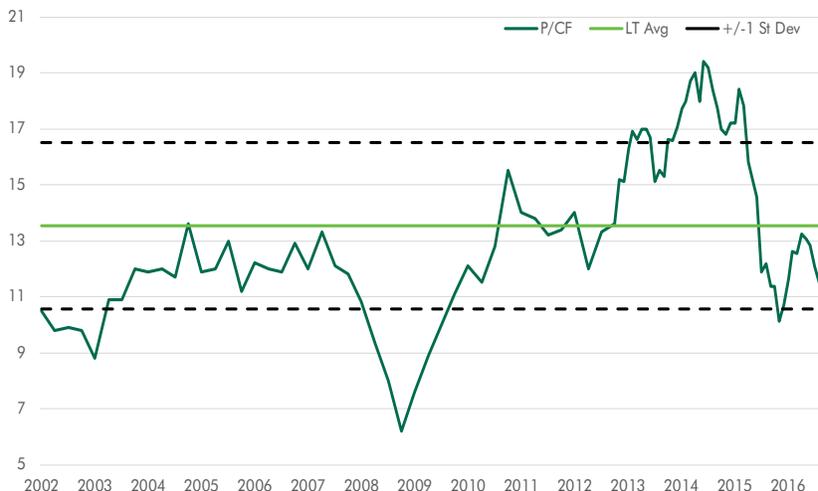
## ATTRACTIVE MLP VALUATION

MLPs trade at a discount in what is a stable and improving fundamental backdrop.

Cash flow multiples are below their historical average across the MLP sector, despite what we consider to be cycle-through cash flows.

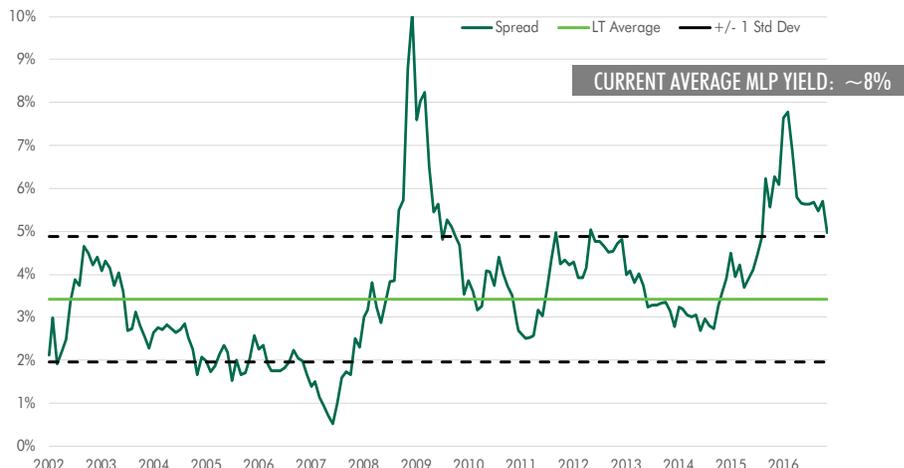
MLPs remain attractive relative to other yield-based securities at nearly 8% yield. The 8% yield is based on distributions that are well-covered by cash flow and are expected to grow in 2017, driving potential for capital appreciation and income.

EXHIBIT 2: MLP PRICE TO CASH FLOW MULTIPLE



Source: CBRE Clarion Securities as of 11/30/2016. Please refer to Important Disclosures on the back page for additional information.

EXHIBIT 3: MLP YIELD SPREAD VS. U.S. 10 YEAR TREASURY



Source: CBRE Clarion Securities, FactSet, Alerian MLP Index as of 11/30/2016. Please refer to Important Disclosures on the back page for additional information.

## TRUMP VICTORY IS THE ICING ON THE CAKE FOR MLPs

Despite fundamental and financial improvements and a return of 58% from February 2016 to the present, the MLP recovery has lagged the recovery in oil prices (Exhibit 4). The election and OPEC outcomes were both clear positives for MLPs, and the valuation gap relative to historical trading levels should correct over time.

With the presidential election decided in favor of less pipeline regulation and with OPEC supporting oil prices, we believe MLPs present an attractive total return proposition that includes more than 7.5% yield and 3-5% annual distribution growth.

EXHIBIT 4: MLP PERFORMANCE

	Peak to Trough	Trough to Present
<b>MLPs</b>		
Peak August 2014	-58%	+58%
Trough February 2016		
<b>Oil</b>		
Peak June 2014	-76%	+89%
Trough February 2016		

Source: FactSet and Alerian MLP Index as of 11/30/2016. Please refer to Important Disclosures on the back page for additional information.

## IMPORTANT DISCLOSURES

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