



**Special QuickTake Podcast with Jen Ashlock, Brian Sulley and Ed Russell  
Nov. 12, 2015**

**Jen Ashlock:** Hi and welcome to a special edition of the QuickTake podcast. I'm here with Ed Russell and Brian Sulley, and we're going to go through some of the questions that we've been getting from the field. And let's start with you Brian. So I'm going to ask the question that everybody is asking. What the heck is going on with MLPs? It feels like this negative market sentiment started when crude oil prices started to fall, and I thought that the price of crude oil and natural gas was not a material factor in midstream MLP business models. So what am I missing?

**Brian Sulley:** Well you really hit the nail on the head when you mentioned market sentiment. Fundamentally, the midstream MLP companies are generally performing well. Third quarter data is coming in, but looking at second quarter, year-over-year, EBITDA has increased by about 10% looking at the MLP indices. So ultimately, the negative market sentiment has been driven more by actual technical factors. You look at the last quarter, that's been increasing short interest in some names out there. You've seen some closed end funds deleveraging, and you've seen more redemptions on the open end fund and ETF side and with very little buyers to balance out the other side of that equation.

**Jen Ashlock:** Great, well that's helpful. Let's move over to Ed and talk about some recent articles that have been published, that suggest that MLPs need access to capital to both grow and maintain distributions. This has caused a lot of concern over potential cuts in midstream MLP distributions. Is this something investors should be concerned about?

**Ed Russell:** Yeah, well we have gotten a lot of questions regarding those articles and we agree with the statement that MLPs need access to capital. That's one way that they fund their growth capex and it is one of the drivers for their distribution growth. What we don't agree with is the assumption that midstream MLPs need access to capital to maintain those distributions. And although the MLP growth outlook maybe more uncertain, we do expect distribution growth in 2016 to be about 5-7% and we see about \$160 billion in growth projects coming online in 2016 -2017. I can give you a little data on Q3 2015 distributions and we're almost done with that and we've seen, at least in the MLP space, 58 MLPs have increased their distribution quarter-over-quarter, 37 of

them have remained flat, and we've seen 6 distributions cuts. And within those distribution cuts, they've been in the exploration and production area or refinery.

**Jen Ashlock:** Great, Brian back to you. Let's talk a little bit about year-to-date performance numbers and the fact that they've been negative across the energy value chain including the midstream, with the exception of refiners of course. Can you walk us through why the market sentiment has been so negative?

**Brian Sulley:** Well in the short term, the entire energy value chain continued to be a little bit more correlated. Particularly correlated with commodity prices, when you're seeing commodity price volatility like we have in 2015. Now the refiners have done better for a couple of reasons. Partially because of the increase in demand for refined products that goes along with lower commodity prices. But also because of some of the differentials that they are seeing in their pricing. As far as the rest of the energy value chain, to some extent they've been caught up in the ride. In that short term, you do see everything go up and down together. You see it more spread out over the long-term, but it's that short-term correlation that can dominate the headlines over the course of a couple of months. Historically, we've seen a couple moving pieces though show us how MLPs move with crude prices, and then over the long-term separate from that a little bit. Particularly, if you look over the last several dips, going back to 2007 and crude pricing, each time, we've seen MLPs move down with crude pricing but ultimately we've seen crude stabilize and then that's followed very quickly by a bounce back in MLP markets.

**Jen Ashlock:** Great, now what factors do you think have led to the crude oil prices falling from their peaks last August and what factors do you think will lead to improved pricing levels?

**Brian Sulley:** Crude pricing can be pretty complicated and there's a number of moving pieces and factors that go into that. You're looking at supply, uncertainty over demand, growth in the future, economics in China and Europe. But, the crux of the story recently really has been about supply. And that goes back all the way to Thanksgiving of last year when Saudi Arabia decided to maintain their production instead of cutting at the OPEC meeting held at that point. So there's been a lot of pressure on prices since last Thanksgiving. We've seen that as prices fell dramatically at that point early in the year. And been fairly volatile over the course of the summer and into the fall. What we're starting to see is some inklings of stability and a bit of a light at the end of that tunnel. We're starting to see a little bit of suggestion of stabilization despite some of the falling production in the U.S. going from a peak of about 9 1/2 million barrels a day, down to about 9.3 million barrels of production a day now and starting to see some inklings of global demand improving a little bit. It's going to provide some stabilization there hopefully in the future.

**Jen Ashlock:** Great. Now everyone has had their eyes and ears on earnings calls lately. Ed, what has your reaction been to the third quarter earnings for midstream

MLPs? And what has Tortoise expected for distribution growth for the sector in 2015 and 2016?

**Ed Russell:** Q3 earnings have generally been positive. Probably been led by natural gas companies favoring the best where we have seen distribution coverage ratios remain strong and growth from the bellwether natural gas MLPs has been very positive. Crude oil and refined product generally has been positive as well although there has been two bellwether names that have caused some investor concerns, that would be Plains All American and on the C-Corp side of things, the Kinder Morgan announcement where they , in that particular case, took guidance down from what was 10% to a range of 6-10%.

**Jen Ashlock:** Okay, so let's go a little bit deeper on that. As far as the equity capital markets being open to MLPs, do you want to comment further on the Kinder Morgan recent preferred offering?

**Ed Russell:** Again, I think if you look at the market sentiment and where MLPs are priced today, you could argue that they're priced in at little to no distribution growth going forward and the Kinder transaction, I think the market's reaction was generally negative when they just looked at the fact that they did a preferred offering at 9.75% when the distribution yield of the equity at the time was 7.5%. But I think what you could look at is the terms of that deal although on its face would appear negative is really a reflection in my opinion that management believes that there stock is cheap today and that in three years it will trading at a better valuation and if that's the case then when that preferred stock converts then this would make it an attractive deal to Kinder, but with the amount of negative sentiment out there in the market, I just don't think that was appreciated. We still believe the capital markets are open for MLPs, but we do expect MLPs to consider alternatives to a traditional equity offering, so we would expect people to look at PIPEs, At-the-Money offerings, or Preferred deals to meet their equity needs in the near future.

**Jen Ashlock:** Let's talk about the most recent announcement when Targa Resources Corp. announced its plans to acquire all the outstanding shares of Targa Resources Partners, L.P. Is this a trend you expect to continue?

**Ed Russell:** We have seen recently a trend of MLPs being acquired by the general partner. Typically to improve distribution coverage or reduce cost of capital. And that certainly could continue. We don't however see this as a sign that MLP structure is broken or out of favor, because we continue to see large energy companies move their midstream assets into the MLP structure. General partner roll-ups would generally be company-specific due to high cost of capital or concerns over growth or coverage ratios, which could be improved by the roll-up of the MLP.

**Jen Ashlock:** So Brian, I'll ask you the most second common question that we get. Do you think this is an attractive entry point for MLP investors?

**Brian Sulley:** In our opinion, valuations are attractive. Regardless of the metric you are using, whether you're looking at yield, price to distributable cash flow, firm value to EBITDA, we're seeing valuations generally below the long-term historical average. And the valuations are attractive particularly when you take anticipated growth into account. But with all that being said, we do continue to see a lot of volatility in the space. Volatility that is not necessarily being dampened by strong performance of the MLP companies themselves. And so, with that in mind, it's definitely an attractive entry point if you're coming into the space with a long-term horizon. Something greater than 12 months.

**Jen Ashlock:** Okay now Ed, we talk a lot about the benefits of owning midstream MLPs, but let's talk about some of the downside risks that investors should consider?

**Ed Russell:** Yeah, so again, this would be in conjunction with owning midstream MLPs, so I want to be very careful when referring to the midstream sector. So, the concerns that we would outline would be exploration and production company borrowing base redeterminations, continued crude oil price volatility, technical pressures that would face the MLP sector and the thing that we're seeing right now in the last couple of weeks, is any surprises from bellwether MLPs, that can tend to generate negative sentiment throughout the market.

**Jen Ashlock:** Let's talk a little bit about closed end funds. For Tortoise's closed end funds, they continue to trade at a discount. The yields seem attractive, but do you have concerns over the funds' ability to maintain its current distribution? And how much leverage do the Tortoise funds carry?

**Brian Sulley:** We have a high degree of confidence that the distribution is sustainable for all the midstream companies that we have in our portfolio. As we mentioned earlier, the companies are doing well in terms of EBITDA growth, they are doing really well in terms of covering their distributions, and growing their distributions. As far as the leverage question goes, leverage will always vary by fund, but generally for Tortoise's midstream portfolios. Leverage is between 20 and 30%. Recently it has been concentrated toward the higher end of that range.

**Jen Ashlock:** Great, Ed can you talk a little bit about fund flows and what we're seeing this year in this volatile market?

**Ed Russell:** Sure, so in regard to our market open end fund products we've seeing positive fund flow. Year-to-date, we have had one month where there was negative fund flow, but absent that one month we're positive for the year. It's a similar story in our SMA product. In that particular product, investors own a basket of MLPs individually. That is typically institutionally held, at least at our shop and again there we have seen positive fund flows with new accounts being opened even with this volatility.

**Jen Ashlock:** So we've given a lot of information today about the midstream. Ed, can you tell us a little about what is Tortoise's outlook for midstream MLPs?

**Ed Russell:** Sure. Our outlook for MLPs remains positive and we view the near-term midstream distributions as secure. We believe that the MLP business model is stable but our focus remains on MLPs or C-Corp companies with the following characteristics. One a midstream focused, large cap, fee-based in nature and investment grade. We would expect distribution growth in the midstream area to be within our range of 5-7% for 2016, and we would also mention that we think investors should have at least a 12 month horizon because we could see some near-term volatility in crude prices which could affect market sentiment.

And again, just to touch base on the concerns that we would have that people should be aware of is borrowing base redeterminations for the exploration and production companies, continued crude oil price volatility effecting market sentiment, technical pressures that we might see in the MLP space and again any surprises from the bellwether MLPs that are out there. But generally, we believe that in the long-term, our outlook is very positive for this sector.

**Jen Ashlock:** Well thanks Ed and thanks Brian for taking time to answer some of the most frequently asked questions that we're getting from the field. And thank you all for joining us for this special edition of the QuickTake podcast.