

Tortoise QuickTake Special Edition Podcast with Ed Russell

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Welcome to a special edition of the Tortoise QuickTake Podcast. Thank you for joining us. Today, Tortoise Managing Director Ed Russell sits down with the Vice President of the Industrial Group, Stifel Nicolaus' Selman Akyol, who covers MLPs to provide a timely update on trending topics in the market.

Ed Russell - Managing Director, Tortoise Capital: Well, I'm here today with Selman Akyol, Analyst from Stifel Nicolaus. Selman, we've seen so much volatility in the MLP space with the average yield currently being over 11%. What do you think the market is really telling us about the MLPs?

Selman Akyol - Vice President, Industrial Group, Stifel Nicolaus: Ed, I think the market is really focused on three things right now. I think number one, they're really questioning whether does the MLP model work? Number two, I think the market is also focused on are distributions going to be maintained, or are they going to be cut? Then lastly, I think you're seeing a huge correlation with oil right now even though historically MLPs do not have that large of a correlation to oil. So, those are the three factors I think right now are really weighing in on the MLPs.

Ed Russell: So, do you agree with that assessment, that MLPs are—distributions are not as sustainable, or do you think there's just more nuance to it than that?

Selman Akyol: Well, first of all, I firmly believe that the MLP model is not terminating. It may be changing, but it's not terminating. Over time, we would expect to see coverage ratios increase, which then means MLPs are retaining more cash, whether to pay down debt or to actually fund any growth projects they would undertake.

We do think the growth capex projects that are out there are trying to be revised. Everyone's trying to push as much to the right as possible. So, we do see growth capex budgets being lower and we do see distribution growth being lower. But by and large, we think distribution has flattened out and that across the board are we seeing cuts. Then lastly, there's a huge focus now on counterparty risk and who's on the other side of your contracts, and how does that bear in this environment, in lower commodity environments.

So, we will see some E&P companies go bankrupt. There's no question about that. It's already underway. But, just because you have a contract with an E&P that goes into bankruptcy doesn't necessarily mean that all those revenues will go away.

Ed Russell: Great. Now, because you're a research analyst, I'll ask especially about what your thoughts are for Q4 earnings, realizing that at this point they're not done completely. But also, can you kind of give us an outlook, that when you talk to your advisors, how are you describing 2016 and what needs to happen to see improvement in the MLP space, or maybe if it's not improvement, just less volatility?

Selman Akyol: Well, as we talk to our advisors, we clearly think the first half of the year is going to be more challenging because we are expecting oil prices to start lifting as you go throughout the year. So, we think really the first six months of the year is the most difficult. As I noted earlier, everything right now seems to be tied to the price of oil. But, I think as we start moving through the year and oil prices start to revamp, that certainly should help the sentiment for the whole group. And so, that would sort of be number one.

But then number two, think about declining oil prices at the E&P level. Remember, prices at the pump, the refined products, you're certainly seeing those come down. So, as prices come down, you're seeing demand life for refined products. So, we've really been focusing our advisors on trying to stay close to demand centers and particularly then we really are focused on the refined products portion of the space.

Ed Russell: What about natural gas? Do you see any differential between the MLPs that are dealing in natural gas versus crude oil or refined product?

Selman Akyol: Yes, in E&P in particular. I mean the gathering process in this space we believe is most challenging. As you know, those MLPs that certainly have more long haul pipelines should be much more insulated, especially those that go out and serve the local distribution companies, otherwise known as LDCs, where those revenues are really generated in fact by utility commissions with the authority to raise rates. So, we see that as being a much more stable part of the market. Clearly, there are MLP by companies that have exposure to that segment. So, there'd be some safety there as well.

Ed Russell: So, Selman, you mentioned counterparty risk, and I know that I'm getting a lot of questions from our investors on that in terms of just what kind of magnitude that would have if you had a customer, an MLP customer file for bankruptcy. Can you kind of talk to me how you're responding to those kinds of questions from your investors?

Selman Akyol: Sure. So first of all, as we go through earning season, we've seen a trend where more and more companies are highlighting their customer base and really trying to quantify and help the investment community understand how much of their revenues are really derived from investment grade ratings and investment grade rated companies. In some instances, it's as high as 85%-plus.

Again, even for those that are not investment grade rated, some of them have to put up additional collateral. We're seeing them get work through that way, and then there are some that are just private companies that even though they don't have an investment grade rating, they say they would be rated investment grade. So, there's certainly that out there as well. But for those companies that do go bankrupt in contrast to your structure, again, at the end of the day, it may not be a zero in terms of the revenue that comes out of it.

Ed Russell: Great. Thank you, Selman. Appreciate it.

Thank you for joining us. And stay tuned for our next cast. Have topics you want covered or other feedback to share? Write us at info@tortoiseadvisors.com

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