
KARLIE KLOSS MAKES TIME TO READ THE WALL STREET JOURNAL.
FIND OUT WHY
THE WALL STREET JOURNAL. Read ambitiously

THE WALL STREET JOURNAL.

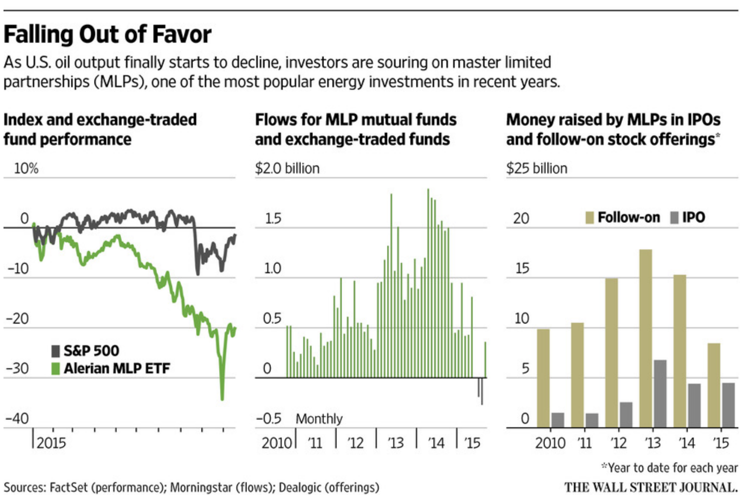
This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers visit http://www.djreprints.com.

http://www.wsj.com/articles/once-hot-master-limited-partnerships-reel-from-sharp-selloff-1445190859

MARKETS | STOCKS | ABREAST OF THE MARKET

Once Hot, Master Limited Partnerships Reel From Sharp Selloff

Drop in MLP shares has outpaced tumble in crude-oil prices



By DAN STRUMPF and CORRIE DRIEBUSCH
Oct. 18, 2015 1:54 p.m. ET

Energy pipeline and storage companies were one of the hottest investments on Wall Street, offering steadily higher payouts, tax benefits and insulation from wild swings in oil prices.

Now, investors are contending with a sharp selloff in master limited partnerships that has outpaced the fall in oil prices. Deal making in the sector has slowed and investors say they are calling into question the ability of MLPs to keep up the steady pace of payout increases as U.S. oil output finally starts to decline.

The yearslong boom in U.S. oil production fueled the proliferation of MLPs. The companies transport, store, produce and refine energy, passing on the bulk of their earnings to shareholders. Income-starved investors flocked to the sector, lured by the companies' assurances of steady payout increases and their tax advantages. Since 2009, MLPs have raised more than $100 billion from initial public offerings and follow-on stock sales, according to Dealogic.

But MLPs have tumbled in price in recent months. The NYSE Alerian MLP Index, a widely tracked barometer for the sector, has lost 25% this year, outpacing the 11% decline in domestic crude prices.

With oil production falling, the need for pipelines is declining, and the sector's multiyear expansion and steady growth in MLPs' dividend-like payments are under threat, investors said. U.S. crude output was down 6% in early October from a recent high in late June, according to government estimates. The number of rigs drilling for crude has fallen sharply, prompting fears that further output declines are on the horizon.

"When U.S. production was growing and financing was cheap, there was an abundance of growth," said John Dowd, manager of the Fidelity Select Energy Portfolio fund, which has $1.8 billion under management. "The outlook is definitely gloomier in the pipeline space than it was six months ago."

Mr. Dowd said he has lightened his holdings of MLPs and other energy companies recently and has moved into shares of certain exploration and production companies, which he said trade at more attractive valuations.

Cuts to payouts are still rare, but they are picking up steam. In the past year, 13 MLPs—nearly all exploration and production companies—have cut the size of their payouts, according to Credit Suisse Group. Payouts for the industry expanded each year between 2010 and 2013, but the growth clip fell to 6% last year, and is forecast to fall again to 5.9% in 2015 and 5.8% next year, according to the bank.

Plains All American Pipeline LP shares have fallen 18% since the energy transportation company said in an August conference call that future payout growth could come under pressure. Linn Energy LLC, the largest oil and gas producer organized as a partnership, earlier this month suspended its payout. Shares are down 70% this year.

Growth expectations were even bigger for some new MLPs at the time of their initial public offerings in the past year.

Pipelines run toward oil-storage tanks in Cushing, Okla. A glut has hit the price of oil -- and of investment vehicles for energy, pipeline and storage companies. *PHOTO: DANIEL ACKER/BLOOMBERG NEWS*

"Investors have correctly started to question these long-term growth forecasts—not just for the dividend itself, but for the ability of the company long-term to grow assets," said Scott Roberts, portfolio manager of the $1.3 billion Invesco High Yield fund.

Because they pass on much of their income to investors, MLPs have historically offered yields well above that of the stocks and bonds of many companies. This year, the $7.7 billion Alerian MLP exchange-traded fund has typically yielded between 5% and 7%, according to FactSet. The benchmark 10-year Treasury note yields 2.026%.

The MLP swoon has tripped up buyers who have stampeded into the sector. They poured more than $19 billion into MLP mutual and exchange-traded funds during the 18 months through June, according to Morningstar Inc. They withdrew a collective $453 million in July and August and in September tiptoed back in.

Before the recent selloff, among the most sought after MLPs have been those of companies that had a parent company ready to keep passing on their assets to a dedicated MLP over time. These "drop-down sales" guaranteed that the MLPs were able to add new income streams and increase payouts. In 2014, Shell Midstream Partners LP and Antero Midstream Partners LP raised more than $1 billion a piece in highly demanded initial public offerings.

These drop downs must be paid for, however, and typically are funded by a mix of capital, equity and debt. Through this time of year in 2014, MLPs raised $19.7 billion in initial public offerings and follow-on equity sales, but this year the figure has fallen to $12.9 billion, according to Dealogic. No MLPs have gone public since June.

"You had a rush of new money into that market," said Curtis Holden, senior investment officer at Tanglewood Wealth Management, a Houston financial adviser who oversees about $825 million. Mr. Holden said he has cut his firm's holdings of MLPs from as much as 4% to a fraction of that amount this year.

Mr. Holden has his eye on buying more if prices stabilize.

"Growth is going to stay lower, but there's still growth potential there," he said.

For some, the recent declines appear to be too steep.

"If we can buy a high-quality name that has a nine or 10% yield and good visibility in terms of what the distribution profile looks like, in this environment I think that works compared with where other yield assets are trading," said Mark Freeman, chief investment officer at Westwood Holdings Group. He said he likes Plains All American Pipeline, Enterprise Products Partners LP and Magellan Midstream Partners LP.

Write to Dan Strumpf at daniel.strumpf@wsj.com and Corrie Driebusch at corrie.driebusch@wsj.com

Copyright 2014 Dow Jones & Company, Inc. All Rights Reserved

This copy is for your personal, non-commercial use only. Distribution and use of this material are governed by our Subscriber Agreement and by copyright law. For non-personal use or to order multiple copies, please contact Dow Jones Reprints at 1-800-843-0008 or visit www.djreprints.com.