January 20, 2017

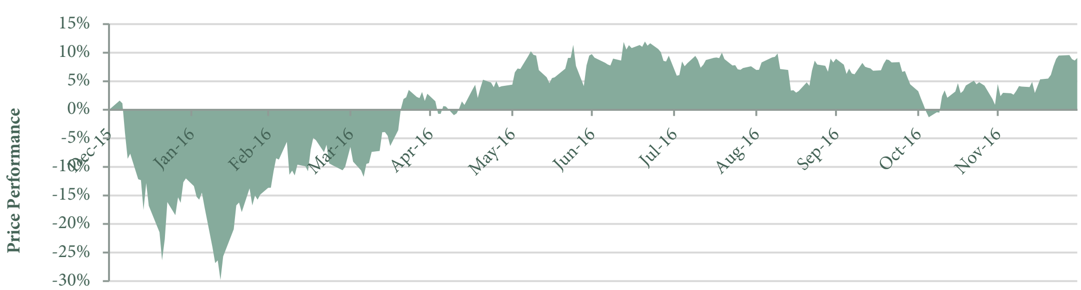
2016 Year End MLP Market Review 2017 Outlook

Dear Investors,

2016 is a year to be remembered, for a multitude of reasons. The volatility encountered during the first quarter was unlike anything we have experienced since the depths of the 2008 financial crisis. Master Limited Partnerships ("MLPs"), as measured by the performance of the Alerian MLP Index (AMZ), began the year with four peak-to-trough moves of ~20% or greater in the first quarter alone – an unprecedented string of movements for the asset class. And although not as extreme, the end of the year finished much like the beginning with the AMZ falling over 10% for the first half of the fourth quarter, only to rebound by over 10% by the end of the year.

As the plethora of concerns reached a crescendo in mid-February, we believed the fears were overblown, or at least more than priced into current equity valuations. We expressed optimism that the market would eventually recognize the resiliency of the midstream model. Although it took longer than we anticipated with more bumps along the way, we feel confident in saying 'we made it through crisis.'

2016 Price Performance of MLPs (as measured by the AMZ)



Note: Represents price performance from January 1, 2016 through December 31, 2016. AMZ is the Alerian MLP Index.
Source: Bloomberg.

With greater commodity comfort and capital market stability, we believe the focus has now shifted to the expected recovery. We now believe the actual "business" of midstream will move back to the forefront with investors, analysts and management teams, including basin presence, integration of asset footprint, project backlog quality, asset utilization and customer optionality, among others.

In this letter, we will elaborate on the following key topics that are driving our optimism for 2017.

- Commodity Price Stabilization and the Volume Recovery.
- Capital Markets, the Evolving MLP Financing Model and the Death of IDRs?
- FOMC Tightening and the Implications of a Rising Rate Environment.
- Compelling Valuations and Multiple Expansion.
- Politics, Regulation, Environmentalists and Tax Reform.
- Key Themes for 2017

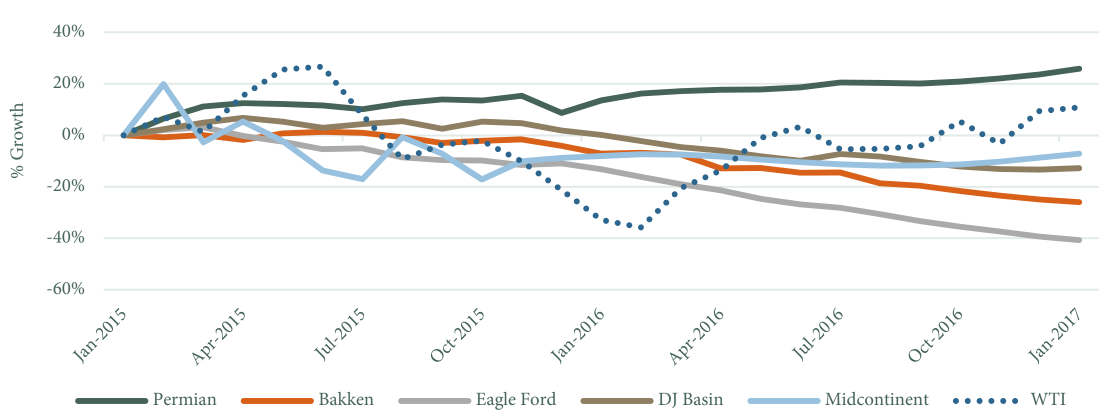
Commodity Price Stabilization and the Volume Recovery.

More than two long years after the Thanksgiving 2014 OPEC decision to leave production unchecked, we can now confidently say that there are clear signs that the bottom of the energy cycle is behind us and the industry is moving into the recovery phase – a very positive backdrop for midstream investing. Analysts from Raymond James made a simple, but logical observation: "*Why are we convinced that 2016 marked the bottom for oil? Simply put, it has become clear that the global oil industry cannot grow aggregate oil supply on a sustainable basis at sub-$50/Bbl oil. The clearest evidence for this is the fact that non-OPEC supply in 2016 posted its steepest annual decline this decade, down 1.3 million bpd (more than 2%) when we compare exit-2016 versus exit-2015… Despite an unrepeatable 2015/16 surge in OPEC supply, the oil supply/demand equation became undersupplied (inventories fell) in the second half of 2016.*" [1]

Early in the down cycle, investors struggled to determine exactly what direct sensitivity MLPs had to commodity prices from an earnings standpoint as the prices of crude oil, natural gas and natural gas liquids fell to decade lows. And, even if most MLPs had no direct sensitivity to commodity prices, there was in many cases the indirect sensitivity related to the inevitable volume declines as a result of decreased exploration & production ("E&P") company activity. For MLP investors, these indirect commodity risk concerns were further exacerbated (particularly in early 2016) by fears of E&P company bankruptcies, counterparty credit risk and midstream MLP contract sanctity. While much damage was done to MLP equities in 2015 and into 2016, we can now say that, in hindsight, traditional midstream cash flows in general were more resilient than many investors initially expected.

As we stand here today, crude oil prices have settled into a more comfortable and economic $50-$55/bbl range following OPEC's significant November 30, 2016 announcement to cut output, which effectively pulled forward the already tightening global supply/demand balance. Domestic rig activity continues to increase from the cycle lows experienced in mid-2016 (particularly in the Permian, SCOOP/STACK, Marcellus/Utica, and Haynseville basins). Production volumes appear to be troughing/inflecting with expected U.S. shale growth increasing for the second consecutive month in February, largely driven by the Permian (with narrowing declines in the Eagle Ford and Bakken basins). [2]

Oil Production Growth by Basin vs. WTI Crude Oil



Source: "Dirty Little Secrets: Lifting the Covers on Midstream Energy Company Risk." East Daley Capital. January 2017.

Of course, volumes are the lifeblood of the midstream business and drive earnings and cash flow. The Bakken and Eagle Ford (crude oil) and Barnett Shale (natural gas) have experienced large declines in this downturn and have

[1] "Midstream Suppliers: 2017 Annual Outlook." Raymond James & Associates. January 12, 2017.
[2] "Drilling Productivity Report: January 2017." U.S. Energy Information Administration. January 18, 2017.

been a focal point of weakness for certain MLPs; however, having diversified business lines and geographic exposure as well as contract protection helped mitigate this for some of the larger midstream companies in recent months. As noted above, declines are narrowing in the Eagle Ford and could actually experience growth later in 2017, a point Kinder Morgan Inc. (NYSE: KMI) management made on their fourth quarter 2016 earnings conference call.

Nonetheless, over the past several months, investors have generally looked past operational weakness and have instead focused on the cyclical recovery, with particular attention on the Marcellus/Utica, Permian, and SCOOP/STACK, where volumes have been increasing. ***If, as some argue, crude oil prices are going to be "capped" near $60/bbl (as an example) due to increasing U.S. shale production, we believe this would be a positive driver for midstream businesses.***

Questions are now centered on better midstream asset utilization (i.e. "free EBITDA" without incremental cap-ex) and when new capacity could be required for areas like the Permian basin. For example, DCP Midstream Partners LP (NYSE: DPM) announced plans to expand its Sand Hills NGL system, and Plains All American Pipeline LP (NYSE: PAA) just announced an expansion of its Cactus crude oil pipeline. For the broader group though, and generally speaking, we would expect new project opportunities to be region-specific and likely smaller in scale than those from pre-2015, underscoring the notion of "haves" versus "have-nots" and stock selection. Further, we believe that if crude oil prices can reach approximately $60/bbl or higher, investors will turn more attention to the second tier basins like the Bakken and Eagle Ford for improving prospects as drilling activity increases.

Often lost in the discussion is the favorable dynamic for natural gas and ethane demand. For natural gas, there is the ongoing build out related to Marcellus/Utica production growth, natural gas fired power generation, liquefied natural gas (LNG) and Mexico exports. For example, RBN Energy states: "Over the next three years, 16 pipeline projects are in the works to add more than 14 Bcf/d of new take-away capacity to move Marcellus/Utica natural gas to the south and west, relieving takeaway capacity constraints that have plagued the Northeast since 2012-13."[3] In addition to new project cash flows, we believe this increasing demand should increase basis differentials in certain areas, enhancing opportunities for pipeline system profits. For ethane, there is a wave of new build/expansions of petrochemical capacity to drive higher ethane pricing which, we believe, should benefit natural gas gathering and processing (G&P) margins. ONEOK Partners LP (NYSE: OKS) projects 886,000 bpd of incremental petrochemical and export capacity through early 2020[4] (with over 500,000 bpd added in 2017 over the 2016 average).

For 2017, we expect the recovery phase of the energy cycle will continue to unfold, with increasing E&P activity, troughing/increasing production volumes, and stable-to-increasing commodity prices. With improving throughput and earnings, this environment is a very positive tailwind for midstream MLP investing, in our opinion. Investors are generally looking past operational weakness and focusing on the cyclical recovery, with particular attention on the Marcellus/Utica, Permian, and SCOOP/STACK basins, where volumes have been increasing. If crude oil pricing can reach approximately $60/bbl or higher, we think investors will look more to second tier areas like the Bakken and Eagle Ford for improving prospects. Questions are now centered on better midstream asset utilization and when new capacity could be required for areas like the Permian. For the broader group, and generally speaking, we believe new project opportunities will be region-specific and likely smaller in scale than those from pre-2015, underscoring the notion of "haves" versus "have-nots" and stock selection.

[3] "I Saw Miles and Miles of Texas - Northeast Natural Gas to Gulf Coast Export Markets." RBN Energy LLC. October 9, 2016.
[4] "UBS MLP One-On-One Conference." Oneok Partners LP. January 10, 2017.

Capital Markets, the Evolving MLP Financing Model and the Death of IDRs?

From a capital markets perspective, the *externally funded* financing model of MLPs came under attack in 2016. Concerns regarding capital funding shortfalls, limited access to debt/equity markets, rising costs of capital, credit rating downgrades and distribution/dividend cuts reached a crescendo during the year, creating significant turmoil within the sector. As we've discussed before, operational performance was not the main problem of 2016, as EBITDA and cash flows were generally resilient for the broader group (as we predicted, and the historical data now proves). However, in the typical MLP structure, the majority of cash flows earned from legacy assets are returned to unitholders in the form of distributions. Therefore, funding requirements for capital expenditures on growth projects are typically funded *externally* via the debt and equity capital markets. Even in a scenario where the underlying fundamentals of an MLP's business remain healthy, a "freezing" of the capital markets, or at least significantly higher debt and equity costs, can quickly lead to fundamental problems, as it did for many MLPs in early 2016.

One year ago, in our fourth quarter 2015 letter, we stated, "*assuming our fundamental thesis holds and our confidence in future earnings proves correct despite current commodity weakness, what is our reasoning for the extreme selling pressure in the asset class? Put simply, we believe capital market concerns, or perceived lack of access to funding, has ignited an epic struggle between company balance sheets, capital spending programs and distributions, leading to unprecedented volatility (and weakness) in MLP equities.*" Little did we know the full extent of the "unprecedented volatility" that would immediately follow these comments in the first quarter of 2016.

In our opinion, the single biggest driver of MLP equity price volatility (and weakness) over the last year was the conflict that arose between different investor types and management teams regarding the optimal allocation of limited capital when the 'well' of new capital 'ran dry.'

We fully appreciate that there are many reasons for the near ~60% peak-to-trough sell off in the midstream asset class from August 2014 through February 2016 (with a $26/bbl low for crude oil among the most obvious!), and of course, we are also aware that the multitude of reasons are often interrelated with a cause-and-effect relationship (i.e. crude oil prices drop, need for new infrastructure declines, E&P counterparty risk increases, CDS spreads spike, cost of capital increases, economics deteriorate, investor sentiment wanes, capital availability weakens, etc.).

In perhaps an overly generic/simplistic example, and assuming a particular company's recurring cash flows were stable (or even growing), an MLP management team typically had the following options when faced with a materially impaired capital market backdrop in 2016:

- ***Satisfy yield-focused equity investors?*** With resilient operational cash flows despite the commodity collapse and an adequate coverage ratio (~1x or greater), there was no immediate need to break the hard earned "trust" between longer-term, yield-seeking investors and management, regardless of current market turmoil and irrational equity yields.
- ***Satisfy the banks and/or debt investors?*** With the equity markets closed, or at least cost prohibitive for the short-term, debt was typically used to shoulder the majority of capital expenditure funding requirements. But there are obviously limits, and there was growing unease among investors regarding rising leverage levels and the possibility of a credit rating downgrade, which could further perpetuate equity weakness (i.e. yields increase further). With rising equity yields, debt holders become concerned with an increasing amount of capital 'walking out the door' in the form of distributions. *The vicious cycle has begun.*
- ***Satisfy total return equity investors?*** With acknowledgement that there were still significant funding requirements for the current backlog of growth projects, raising equity capital at mid-teen yields (or worse) to fund mid-teen IRR projects would be a futile endeavor at best, and dilutive at worst. Debt financing was

becoming increasingly limited, and new capital must be raised somehow. Recurring cash flows from operations remained resilient, but these cash flows continued to be distributed to equity holders. *Was this the best, highest net present value use for these cash flows?*

Fortunately, the second half of the year (and first few days of 2017) brought about resolutions to the majority of the concerns regarding capital markets availability, cost of capital and the allocation of capital that plagued the MLP space in early 2016. The vast majority of MLPs chose to maintain, and actually grow their distributions throughout the crisis, building investor confidence in their ability to withstand energy sector turmoil. The select and notable distribution cuts that, in our opinion, needed to occur are now complete. Some midstream companies abandoned the *externally funded* financing model entirely (notably KMI), and will now *internally fund* capital backlogs for at least the intermediate term, while others took a more balanced / hybrid approach with higher coverage (PAA, Williams Partners, LP (NYSE: WPZ), NGL Energy Partners, LP (NYSE: NGL), among others).

The lesson from the crisis is clear. We believe both management teams and investors are now more cognizant of the underlying risks and complications of a solely externally funded capital structure. Going forward, we expect MLPs to pursue a more balanced approached to capital expenditure requirements (i.e. a blending of internal and external funding).

With the crisis fresh in their memories, we expect management teams will continue to take actions to prevent their businesses from being beholden to the, at times, "chaotic" behavior of the equity capital markets. Of course, management teams cannot prevent a similar market panic in the future; however, we believe less dependence on capital markets going forward will go a long way to preventing a short-term panic from leading to more lasting fundamental problems, as it did in early 2016. We believe this will ultimately result in higher coverage ratios and less capital being immediately returned to unitholders in the form of distributions. However, we also believe equity holders will appreciate the more measured and balanced approach to future funding requirements, as less equity needs could ultimately result in higher distribution growth potential longer term (i.e. higher total return).

The second lesson from the crisis is the paramount importance of a competitive cost of capital. Rising equity yields (as mentioned above) are one component of this; however, incentive distribution rights (IDRs) are a second, and more controllable component of an MLP's cost of capital. To put it succinctly, we believe IDRs are an unsustainable long-term burden on the cost of capital for maturing MLPs, and we expect the few large cap MLPs with IDRs still outstanding to eventually collapse their structures as well. Of note, we have had three more "simplification" transactions announced in the first two weeks of 2017.

As we begin 2017, it appears the energy capital markets are open, reasonably healthy and working again. Most MLP management teams have taken considerable actions to optimize the allocation of capital, reduce capital costs, simplify their corporate structures and better position their respective companies for the energy cycle recovery. We expect management teams to have a renewed focus on capital efficiency and the return earned on invested capital. Moving forward, we believe a company's cost of capital will be one of its best "weapons" in competing for growth projects in the recovering energy cycle, and as such, we expect midstream companies will continue to pursue transactions that will reduce their cost of capital.

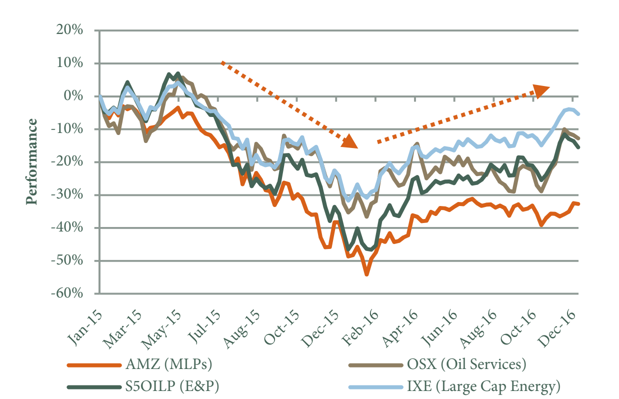
With financial improvements well underway and cost of capital concerns addressed, we believe MLP management teams will be positioned once again to capitalize on organic growth and acquisition opportunities in 2017. We believe this dynamic, coinciding with our expectations for a volume recovery, an increasing rig count and the return of infrastructure demand, establishes a very favorable backdrop for the midstream asset class.

FOMC Tightening and the Implications of a Rising Rate Environment.

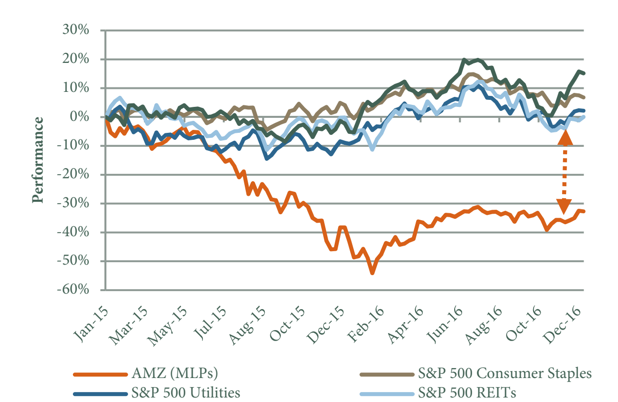
Given the Federal Open Market Committee's (FOMC) decision to raise the Federal Funds Target Rate by 25 bps at the end of last year and the expectation for further hikes in 2017, investors are beginning to question the potential headwinds arising from an increase in long-term bond yields, and specifically their impact on yield-oriented asset classes (including MLPs). We have written extensively in the past regarding the historical lack of correlation between MLP yields and that of the 10-year treasury yield (please contact us if you would like to see the full analysis). But to summarize, we continue to contend that there has historically been very little correlation between MLP yields and long-term bond yields (outside of short-lived rate "shocks," which can also affect broader market equities in general).

Other yield-focused asset classes, notably REITs and Utilities, have historically traded with a much higher/tighter correlation to interest rates and long-term bond yields, making these asset classes much more of a "bond proxy." Recently, as yields fell to a multi-decade low in July of 2016 (the U.S. 10-year Treasury yield hit a low of 1.36% on July 8, 2016), these same asset classes rose to all-time highs and valuations. Unfortunately, these record low yields offered little solace to MLPs, which were still struggling with an array of sector concerns discussed elsewhere in this letter. For better or for worse, MLPs yields were significantly more correlated to crude oil prices (particularly when at extreme levels – both high and low) and the overall energy sector than they are to the 10-year U.S. Treasury. One only needs to look at relative performance over the last two years (below) to appreciate this dynamic.

Performance of Energy Indices [1][2][3]



Performance of Yield-Focused Indices [1][2][3]



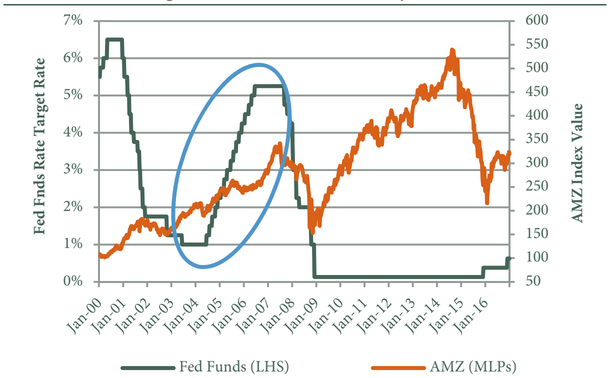
1) Source: Bloomberg, Returns shown for the period from January 2015 through December 31, 2016. **PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.**
2) Represents price return.
3) See Glossary of Indices on p. 14 for additional information regarding each index.

Sometimes this "relationship to crude" works to the detriment of MLP investors, as it did since the beginning of the energy down cycle in the 2nd half of 2014. However, at other times, and we believe this could certainly be one of those times, this can work as an advantage. We agree with the conclusions of Steve Fleishman, a research analyst at Wolfe Research, who states it well. "*MLPs are the only income sector outperforming the market since Trump won the election. This highlights one of the main benefits of owning MLPs – they are the only income sector that is* <u>*not*</u> *a bond proxy. Bond yields have jumped 50bps since the election driving utilities, staples and REITs down with them. This may be a wake-up call to income investors that they are taking an embedded macro risk that interest rates stay low. MLPs can provide diversification to this - they are income stocks that are more of an oil proxy than a bond proxy.*"[5]

[5] Fleishman, Steve. *Midstream of Consciousness: It's nice not to be a bond proxy.* Wolfe Research. November 20, 2016.

Our point is further strengthened when analyzing previous FOMC tightening cycles and their impact on the performance of MLPs, although admittedly, relevant historical data is limited. Beginning in June 2004, the FOMC began a series of 17 consecutive 25 bps rate hikes, ultimately increasing the Federal Funds Target Rate from a four decade low of 1.00% to 5.25% by June 2006. Over this same timeframe, MLPs, as measured by the AMZ, experienced a total return of almost 40%, strongly outperforming the S&P 500 Index total return of 16.4% for the period. Why was the performance of MLPs so strong over this time period? At risk of stating the obvious, MLP outperformance was driven by positive developments in the energy sector including the emergence of shale plays, horizontal drilling techniques, commodity price strength, etc. Over this same time frame, the yield spread of MLPs to the 10-year U.S. Treasury actually spent time in negative territory (note the spread ended 2016 over 450bps versus a long-term average of over 300bps). Case in point, we continue to believe the future performance of MLPs will be more determined by the underlying fundamentals and trends within the energy sector, on which we remain very constructive.

Fed Funds Target Rate, 10-Yr Treasury and AMZ (1)(2)

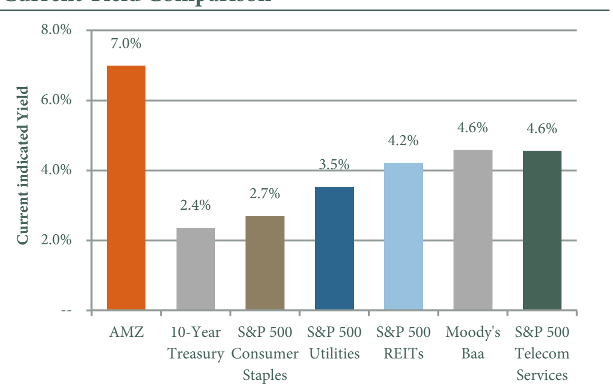


1) Source: Bloomberg. As of December 31, 2016.
2) Represents price return.

As it relates to the impact of rising rates on MLPs' cost of capital, we do not believe an *orderly* rise in interest rates will have a materially adverse impact on financing costs. However, and given the capital-intensive characteristics of the asset class, this is something we diligently monitor for every company in our space as part of our bottom-up research process (leverage ratios, fixed/variable rate debt, capital expenditure needs, ROIC, etc.) As we mentioned earlier, we believe the reopening of the capital markets, the normalization of debt and equity yields and the improvement in balance sheets within the sector will more than offset the negative impacts of an orderly rise in interest rates. Lastly, if financing costs do increase in the future, we trust that management teams will appropriately adjust their required rate of return on future projects for their effective cost of capital, maximizing return on invested capital for their shareholders. Note, we also intend to avoid any companies that are unsuccessful in doing so.

For 2017, we do not believe a rising rate environment will be a significant headwind for MLPs. Historically, MLPs have been less correlated to interest rates, and more correlated to energy fundamentals, including commodity prices, production trends, infrastructure demand, etc. With the belief that the bottom of the energy cycle is behind us, we believe MLPs provide investors with a highly compelling combination of an attractive yield (both on an absolute basis and relative to historical levels), attractive valuations, a positive fundamental backdrop and exposure to the recovering energy sector.

Current Yield Comparison (1)(2)



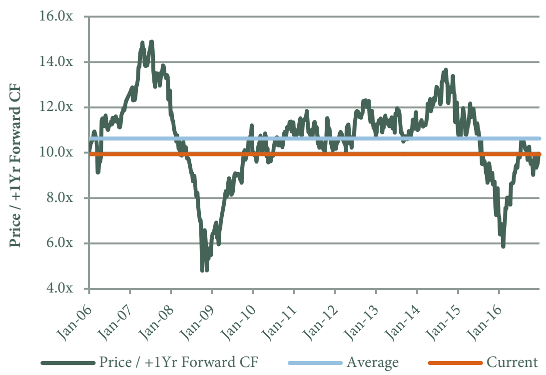
1) Source: Bloomberg, as of December 31, 2016.
2) See Glossary of Indices on p. 14 for additional information regarding each index.

Furthermore, we believe a rising rate environment has the potential to create a fund flow tailwind for MLPs, as yield-seeking investors rotate away from more expensive, lower yielding and more interest rate sensitive (i.e. bond proxy) assets classes such as REITs and utilities and into midstream energy infrastructure.

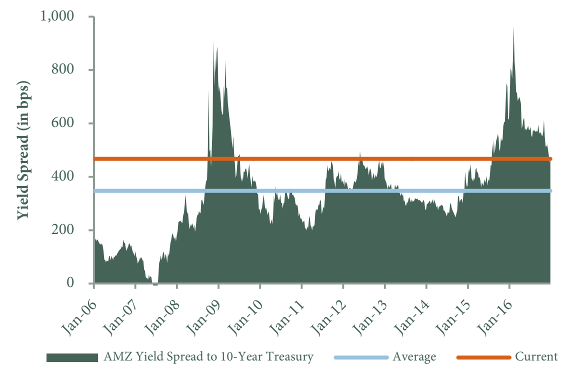
Compelling Valuations and Multiple Expansion.

As we shift to the anticipated recovery and a re-focus on MLP business fundamentals, we believe current valuations for MLPs remain compelling. Relative to MLPs' trading history, we believe MLPs, as measured by the index, screen very attractive based on P/DCF and yield spread valuation metrics.

AMZ Price to +1Yr Forward Cash Flow (1)



AMZ Yield to 10-Year Treasury (1)

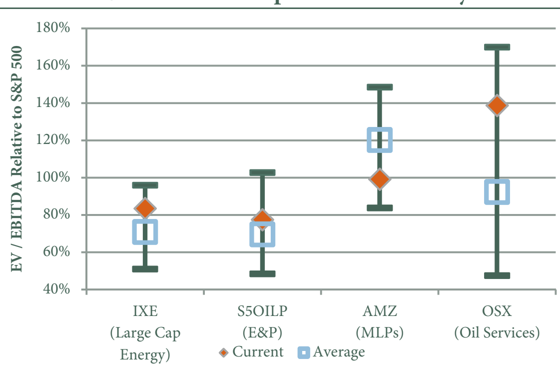


1) Source: Bloomberg, as of December 31, 2016. **PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.**

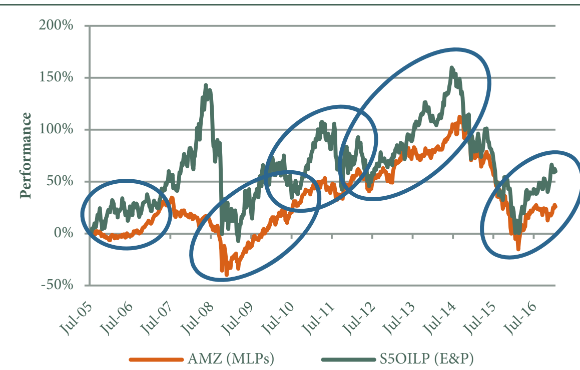
At worst, MLPs screen as fairly-valued based on EV/EBITDA metrics, which we expect to continue to improve as leverage works its way down and EBITDA ramps into the second half of 2017 as a result of volume growth and project completions. Regardless, MLPs look significantly less expensive relative to EV/EBITDA multiples for the broader energy group as measured against the S&P 500 Index (shown in the chart below left). ***Unlike the MLP sector, as of the end of the year, these energy sectors were trading above average levels in relation to the broader equity market, an indication, we believe, that the market is anticipating an earnings recovery. MLPs continued to trade at a discount to average levels, despite the potential for a similar earnings recovery.***

Over the course of the energy correction, there was little differentiation across the industry as midstream energy stocks fared worse than other segments of the energy supply chain despite more stable earnings. Further, the AMZ has not kept pace with these sectors in the subsequent recovery. Accordingly, we believe this presents the opportunity for further multiple expansion in 2017, and MLPs may experience a 'catch up' trade relative to the other energy sectors in the coming year (see chart below right).

Relative EV / EBITDA Multiples Versus History (1)(3)



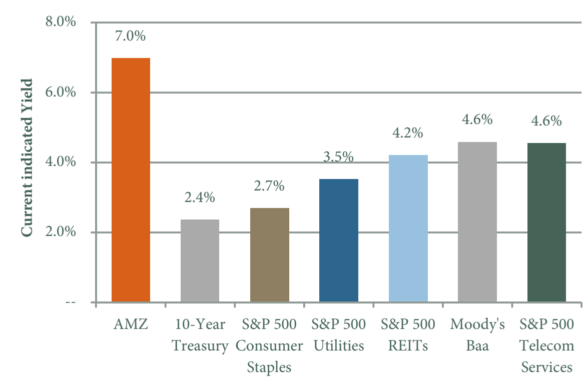
Performance of MLP and E&P Indices (2)(3)



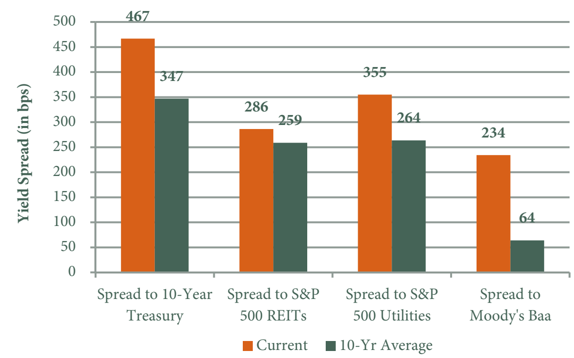
1) Source: Bloomberg, as of December 31, 2016.
2) Source: Bloomberg. Performance shown for the period from July 1, 2005 through December 31, 2016.
3) **PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.** See Glossary of Indices on p. 14 for additional information regarding each index.

While the global search for yield has inflated valuations for utilities, REITs and other yield-alternative asset classes, MLPs' correlation to energy and crude oil (i.e. negative performance) has resulted in the widening of yield spreads to these yield alternatives. ***We believe MLPs provide investors with a highly compelling combination of an attractive relative yield, distribution growth (street consensus for the index of ~4% for 2017)[6], less sensitivity to rising interest rates and exposure to a recovering energy sector.***

Current Yield Comparison (1)(2)



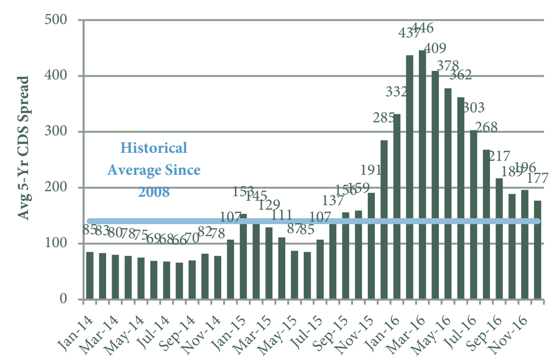
Current vs Historical Yield Spreads (1)(2)



1) Source: Bloomberg, as of December 31, 2016. **PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.**
2) See Glossary of Indices for additional information regarding each index.

For 2017, we believe improving macro fundamentals and investor sentiment provide a supportive backdrop for multiple expansion in the midstream sector, paving the way for attractive equity price performance, both relative to the broader energy sector and yield-oriented asset classes. With expected increases in E&P capex for well connects and drilling activity, we also anticipate a volume recovery for the midstream sector, and even a return of volume growth heading into the second half of 2017. This volume growth should lead to an earnings recovery, setting the stage for positive earnings revisions and continued multiple expansions.

Average 5-Yr CDS Spread of Investment Grade MLPs (1)



1) Blum, Michael. Wells Fargo MLP Monthly: January 2017. Wells Fargo. January 6, 2017.

Perhaps most importantly, we believe the current discount of the midstream sector (as compared to other energy sectors and high-yielding asset classes), to wane as capital markets strengthen and investors re-shift their focus back to fundamentals. While energy high yield spreads led on the downside, we see the continued easing of credit conditions as a significant potential tailwind for the upside.

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[6] Source: Bloomberg.

Politics, Regulation, Environmentalists and Tax Reform.

A key new theme, as evidenced by the positive market reaction following the presidential election, is President Trump's focus on increased infrastructure spending and reduced federal regulation, which should create a favorable and proactive environment for midstream energy transportation companies.

Perhaps the highest profile recent example of how the current administration's political biases have directly affected MLPs comes from the Dakota Access Pipeline (DAPL), a joint venture project in which MLPs Energy Transfer Partners, L.P. (NYSE: ETP), Sunoco Logistics Partners L.P. (NYSE: SXL) and Enbridge Energy Partners, L.P. (NYSE: EEP) participate along with Marathon Petroleum Corporation (NYSE: MPC) and Phillips 66 (NYSE: PSX). On November 14, 2016, the Army Corps of Engineers deferred a decision on granting an easement to cross under Lake Oahe in North Dakota in order to pursue additional discussions with the Standing Rock Sioux Tribe (SRST) that opposes the pipeline.[7] Subsequently, on December 4, 2016, the Corps announced that it was declining to approve the easement in order to investigate alternate routing, indefinitely delaying completion of the final 1,094 feet of the 1,172 mile pipeline.[8]

In an interview with Chris Wallace of Fox News aired on December 11th, Donald Trump appeared to be supportive of allowing DAPL to be completed without offering any specifics as to how that would happen. When asked by Wallace whether he would start DAPL, Trump offered, "*I'm not saying anything. I just say something will happen, and it'll be quick. I think it's very unfair. So it'll start one way or the other*."

For their part, the joint venture partners and many industry analysts are optimistic that the easement will be granted in short order under the new Trump administration. Once the easement is granted, ETP has said that it would need 90-120 days to complete the crossing.[9]

Trump has also promised "a decision" on the Keystone XL Pipeline, a project by TransCanada Corporation (TSX: TRP), owner of the general partner interest of MLP TC Pipelines, LP (NYSE: TCP).[10]

It appears to us that the broader read for MLPs based on expectations from the Trump administration is decidedly positive. Trump's *Contract with the American Voter*, released on October 22, 2016, pledges to reverse "Obama-Clinton roadblocks" hindering energy infrastructure projects, and calls on Congress to pass legislation to spur $1 trillion in energy and infrastructure public-private investment over 10 years.[11] He has furthermore made cabinet nominations in the Environment, Interior, Energy and State departments who are either energy industry participants (Rex Tillerson, Rick Perry) or who have in past government service adopted stances and taken actions supportive of energy development (Perry, Ryan Zinke, Scott Pruitt). The expectation amongst most observers is that these individuals, once confirmed, will run their departments in a manner friendly to the energy industry.

The Republican-majority Congress could also have a say in reducing the regulatory burden on infrastructure, including potentially passing legislation that speeds the timeline for regulatory review of pipeline projects. The review framework under which the Federal Energy Regulatory Commission (FERC) operates is set by statute, so only Congress has the power to reduce the review timeline.

[7] Darcy, Jo-Ellen. Letter to the Honorable Dave Archambault II, Kelcy Warren and Joey Mahmoud. November 14, 2016.
[8] "Army will not grant easement for Dakota Access Pipeline crossing." U.S. Army. December 4, 2016.
[9] Gordon, Meghan and Allen Reed. "Dakota Access startup likely in H2 2017." *Oilgram News*. S&P Global Platts. December 6, 2016.
[10] "Exclusive: Donald Trump on Cabinet picks, transition process." Transcript from Fox News Sunday. December 11, 2016.
[11] *Donald Trump's Contract with the American Voter*. http://donaldjtrump.com/contract.

Nonetheless, while the tone and action out of Washington, DC is likely to be more infrastructure friendly, we expect continued resistance from environmentalists as well as ongoing headwinds with certain state and local level groups. Whether related to oil or natural gas infrastructure, environmentalists have surely felt emboldened by the political success from fighting DAPL, and we have recently seen similar tactics employed with other assets/projects. Further, we expect certain parts of the country, namely the northeast, to continue to be more challenging for developing new projects—accordingly, management teams have to generally budget more time and cost to build. We have already seen a number of projects in the northeast face delays or outright cancellation (e.g. Spectra Energy Partners LP's (NYSE: SEP) Access Northeast project is effectively on hold).

In addition to the aforementioned proposed cabinet appointments, Trump will have the authority this year to nominate, with Senate confirmation, three new FERC commissioners (out of a total of five) as well as designate the chairman. The FERC regulates interstate pipelines, among other things, and is currently comprised of only three Democrats. While we believe the Trump election is an incremental positive, we note that the FERC has historically been MLP/infrastructure friendly. There are, however, two unresolved issues at the FERC that have the potential to negatively impact pipeline earnings. The first is whether the FERC changes policy related to the income tax allowance (ITA) (currently, FERC regulated pipelines are allowed to recover an income tax allowance under a cost of service framework). Our current understanding is that a negative outcome would not be significantly detrimental to the MLP space given the number of FERC regulated pipelines owned by MLPs with (a) cost of service contracts and (b) earning maximum allowable rates. The second outstanding issue is the FERC is currently evaluating whether to change the methodology used to index oil pipeline tariffs. For both issues, we will have to wait and see what the outcome is, but the new makeup of the commission could have a favorable impact.

Another area of potential concern to MLP investors may come from efforts in Congress to reform corporate taxes. While we believe there is a low risk that the MLP vehicle itself would be eliminated through a corporate tax reform package, the MLP structure (specifically its cost of capital) may become *less advantageous* relative to their C-corp peers. The headline for this effort is a reduction in the top corporate income tax rate from 35%, but perhaps not as low as Trump's proposed 15% rate or the 20% proposal advanced by House Republicans.[12] However, since MLPs are pass-through entities not subject to federal income taxation, the benefits of corporate tax reform would not, in general, accrue to MLP investors. Regardless, this kind of reform takes considerable time, and it is simply too early to speculate on the final outcome.

For 2017, we believe the unexpected Trump victory, coupled with the Republicans maintaining their majorities in the Senate and the House, is significant and clearly a positive development for the energy sector and MLPs, and one we think will dominate the investor mindset. We believe it is likely that legislative support for the energy industry will be strong, and that regulatory hurdles will be reduced. President Trump's cabinet will likely have several members who are unabashed supporters of the oil and gas industry. We expect that for at least the next several years, government policy will be more consistent and positive for energy exploration and development – ultimately leading to increased levels of drilling and exploration activities.

There are other issues that bear watching: 1) ongoing environmentalist activism, 2) state-level opposition to certain infrastructure projects, 3) how the FERC ultimately rules on the income tax allowance as well as the oil pipeline index ratemaking methodology, and 4) broader tax reform and what, if any, impact these events have on MLP performance.

[12] "Tax." *A Better Way: Our Vision for a Confident America.* House Republican Party Tax Reform Task Force. June 24, 2016.

Conclusion and Key Themes for 2017.

We were not disappointed to see 2016 move into the history books. It was an incredibly tough year all around: for the energy sector, for the midstream 'model', for management teams and investors.

With greater commodity comfort and capital market stability, we believe the focus has now shifted to the anticipated recovery. We are optimistic that the actual "business" of midstream will move back to the forefront with investors, analysts and management teams, including basin presence, integration of asset footprint, project backlog quality, asset utilization and customer optionality, among others.

What is our outlook for the year ahead? We believe:

- ***Prices for both crude oil and natural gas have experienced their low for the current cycle.*** The major supply-side issues appear to have been corrected, and we expect continued improvement throughout the year.
- ***New sources of demand come online, offering further commodity support.*** Ethane crackers, export facilities (LNG/ethane), natural gas exports to Mexico… demand responded and is (finally) coming online.
- ***U.S. productions levels will trough in early 2017, and will climb throughout the year.*** In addition to well connects and DUC completions, E&Ps will once again redeploy rigs and increase drilling activity.
- ***Volumetric growth will return for midstream companies.*** Underutilized midstream capacity will begin to fill, generating increased EBITDA with little to no capital investment (i.e. "free EBITDA")
- ***Midstream earnings recovery will lead to multiple expansion.*** Volume growth should lead to an earnings recovery in 2H 2017, setting the stage for positive earnings revisions and multiple expansion.
- ***Mergers and acquisitions within the space will continue.*** The sector is ripe for consolidation, and with the improvement in capital markets and balance sheets, management teams are now able and willing.
- ***Cost of capital will reign supreme.*** Management teams will continue to look to reduce capital costs, simplify their corporate structures and better position their companies for the energy cycle recovery.
- ***Investors re-focus on fundamentals.*** We expect forward performance to be more defined by midstream-specific competitive dynamics, a welcome change from the prior macro-dominated period of fear.
- ***Preference for growth.*** As valuations and yields for "fix it" midstream companies continue to normalize, investors will rotate back into higher growth names (high growth significantly underperformed in 2016).
- ***Political headwinds shift to tailwinds.*** While supply/demand fundamentals will still dictate energy needs, we expect the pro-domestic energy / less regulation stance of the incoming administration to be positive.
- ***Environmentalist uprising.*** Environmentalists feel emboldened by the political success from fighting DAPL, and we doubt this will be the only battle. We will be monitoring this movement closely.
- ***Investor sentiment improves, fund flows return to the asset class.*** With attractive valuation, an improving commodity landscape, volumetric and earnings growth and new project announcements, investors will redeploy new money into the space, improving capital market costs and availability. A *virtuous* cycle begins.

In case you can't tell, we are rather optimistic on the year ahead.

As always, we appreciate your support. Thank you for your continued confidence. Please call us with any questions or comments.

Cushing Investment Team

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Investments in MLPs are subject to price changes in crude oil and natural gas, as well as regulatory and interest rate risks, among others.

Glossary of Indices: The Alerian MLP Index (AMZ) is a composite of the most prominent energy master limited partnerships. The S&P 500 Oil & Gas Exploration and Production Sub Industry Index (S5OILP) is comprised of stocks in the S&P Total Market Index that are classified in the GICS oil & gas exploration & production sub-industry. The Philadelphia Stock Exchange Oil Services Sector Index (OSX) is a price-weighted index composed of 15 companies that provide oil drilling and production services, oil field equipment, support services and geophysical/reservoir services. The S&P Energy Select Sector Index (IXE) is a modified capitalization-weighted index comprised of stocks within the GICS energy sector of the S&P 500 Index. The index is intended to track the movements of companies that are components of the S&P 500 and are involved in the development or production of energy products. The S&P 500 Utilities Index is comprised of stocks in the S&P 500 Index that are classified as members of the GICS utilities sector. The S&P 500 Real Estate Investment Trusts REITS Industry Index (S&P 500 REITS) is comprised of stocks in the S&P 500 Index that are classified as members of the GICS REITs sector. The S& P 500 Consumer Staples Sector Index (S&P 500 Consumer Staples) is comprised of stocks in the S&P 500 Index that are classified as members of the GICS consumer staples sector. The S&P500 Telecommunications Services Index (S5TELS) is a capitalization-weighted index comprised of stocks in the S&P 500 Index that are classified as members of the GICS telecommunications sector. The Moody's Corporate B Bond Index (MOODCBAA) is a long-term corporate bond yield average derived from pricing data on a regularly replenished population of Baa corporate bonds in the U.S. market, each with current outstandings over $100mm. The bonds have maturities as close as possible to 30 years; they are dropped from the list if their remaining life falls below 20 years. The U.S. Generic Government 10-Year Yield (USGG10YR) is comprised on Generic U.S. on-the-run government bond indices. Yields are yield-to-maturity and pre-tax. S&P 500 Index is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Indices are included for comparative purposes only.

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